

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF BULLOCK PEN WATER )  
DISTRICT FOR A CERTIFICATE OF PUBLIC )  
CONVENIENCE AND NECESSITY TO CONSTRUCT )  
PROPOSED WATERWORKS IMPROVEMENT ) CASE NO.  
PROJECT AND FOR APPROVAL OF PROPOSED ) 2008-00170  
PLAN OF FINANCING, INCREASE IN RATES, )  
NONRECURRING CHARGES, AND TARIFF )  
REVISIONS )

ORDER

On July 7, 2008, Bullock Pen Water District (“Bullock Pen”) applied for a Certificate of Public Convenience and Necessity (“Certificate”) to construct a \$2,614,600 waterworks improvement project, for authority to enter into a loan agreement with the Kentucky Infrastructure Authority (“KIA”) for \$2,434,600, for authority to increase its water rates, for authority to increase certain nonrecurring charges, and for approval of the completely revised, comprehensive tariff. Because of filing deficiencies, the Commission did not accept the application for filing until February 18, 2009. On April 15, 2009, the Commission granted the Certificate and authorized the proposed KIA loan.

Commission Staff, having performed a limited financial review of Bullock Pen’s operations, has prepared the attached report containing its findings and recommendations regarding the proposed water rates, nonrecurring charges, and tariff revisions. All parties should review the report carefully and submit any written

comments about Staff's findings and recommendations or requests for a hearing or an informal conference no later than 14 days from the date of this Order.

IT IS THEREFORE ORDERED that:

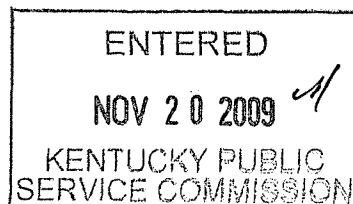
1. All parties shall have 14 days from the date of this Order to submit to the Commission written comments, if any, regarding the attached Staff Report and to request a hearing or an informal conference in this matter.

2. Any party requesting a hearing in this matter shall state in its request its objections to the findings set forth in the Staff Report and provide a brief summary of testimony that it would present at hearing.

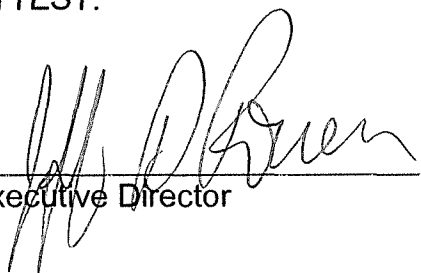
3. A party's failure to object to a finding or recommendation contained in the Staff Report within 14 days of the date of this Order shall be deemed as agreement with that finding or recommendation.

4. If no request for a hearing or an informal conference is received within 14 days of the date of this Order, this case shall stand submitted to the Commission for decision.

By the Commission



ATTEST:

  
\_\_\_\_\_  
Executive Director

STAFF REPORT  
ON  
BULLOCK PEN WATER DISTRICT  
CASE NO. 2008-00170

Bullock Pen Water District (“Bullock Pen”) applied for a Certificate of Public Convenience and Necessity (“Certificate”), for authority to enter into a loan agreement with the Kentucky Infrastructure Authority (“KIA”), for authority to increase its water rates, for authority to increase certain nonrecurring charges, and for approval of the completely revised, comprehensive tariff. In its April 15, 2009 Order, the Commission granted Bullock Pen’s Certificate and authorized the KIA loan. This Staff Report addresses the issues of the proposed increase in water rates, proposed increases to the nonrecurring charges, and the proposed tariff revisions.

In order to evaluate the requested increase, Commission Staff performed a limited financial review of Bullock Pen’s test-period operations. In its July 7, 2008 application, Bullock Pen proposed to use the calendar year 2007 as the test period.<sup>1</sup> Given that the application was not considered filed until February 18, 2009, Staff used as the test period in this proceeding the most current financial information available, the calendar year ending December 31, 2008.

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

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<sup>1</sup> Application, Exhibit 9, Financial Statements for the Years Ended December 31, 2007 and 2006.

Mark Frost and Jason Green of the Commission's Division of Financial Analysis performed the limited review. This report summarizes Staff's findings and recommendations. Mr. Green calculated the pro forma revenue adjustment using the 2008 billing analysis supplied by Bullock Pen. He is also responsible for the calculation of the rates that Bullock Pen could justify, and the proposed increases to the nonrecurring charges. Mr. Frost is responsible for pro forma surcharge calculations, all pro forma expense adjustments, and the revenue requirement determination.

The comparison of Bullock Pen's actual and pro forma operations is attached hereto as Appendix A.<sup>2</sup> Based upon the recommendations and findings of Staff's limited review of the operating revenues and expenses reported in the 2008 Annual Report and Bullock Pen's responses to Staff's information requests, Bullock Pen's pro forma operating statement appears as set forth in Appendix B. The discussions of Staff's proposed pro forma adjustments are shown in Appendix C.

As of December 31, 2008, Bullock Pen reported that it had 16 long-term debt issuances outstanding. In this proceeding, the Commission has authorized Bullock Pen to obtain a new KIA loan to fund the Phase 6 construction project. Using the amortization schedules<sup>3</sup> for the outstanding debt and calculating the annual debt service for the new KIA loan, Staff arrives at its three-year average debt service payment of \$738,352 as shown in Table 1 below.

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<sup>2</sup> Bullock Pen's Response to the Commission Staff's Second Information Request, Item 3(a).

<sup>3</sup> Id., Item 18(b).

| Series                       | 2009              | 2010              | 2011              | Totals<br>2009 - 2011 |
|------------------------------|-------------------|-------------------|-------------------|-----------------------|
| RD, Series 1978              | \$ 79,050         | \$ 79,500         | \$ 78,800         | \$ 237,350            |
| RD, Series 1982              | 7,550             | 7,350             | 7,150             | 22,050                |
| KRW, Series 2001C            | 27,107            | 26,592            | 26,077            | 79,776                |
| KRW, Series 2001C            | 25,508            | 24,993            | 24,993            | 75,494                |
| KRW, Series 2001G            | 40,733            | 40,758            | 40,661            | 122,152               |
| KRW, Series 2002B            | 45,697            | 45,675            | 45,581            | 136,953               |
| KRW, Series 2004D            | 8,741             | 8,538             | 8,336             | 25,615                |
| KRW, Series 2005B            | 19,699            | 19,371            | 19,044            | 58,114                |
| KRW, Series 2005B            | 34,735            | 34,162            | 33,589            | 102,486               |
| KIA, 1991 Loan #1            | 27,905            | 26,786            | 13,105            | 67,796                |
| KIA, 1991 Loan #2            | 37,067            | 35,724            | 36,807            | 109,598               |
| 2002 KIA Loan (DWSRF #1)     | 25,169            | 25,169            | 25,169            | 75,507                |
| KaCOLT, Cap. Lease #1        | 113,092           | 112,399           | 112,494           | 337,985               |
| KaCOLT, Cap. Lease #2        | 26,798            | 26,833            | 26,817            | 80,448                |
| Old Nat. Bank, Cap. Lease #1 | 60,457            | 60,457            | 60,457            | 181,371               |
| Old Nat. Bank, Cap. Lease #2 | 27,817            | 27,817            | 6,954             | 62,588                |
| KIA DWSRF Loan - Proposed    | 146,591           | 146,591           | 146,591           | 439,773               |
| Totals                       | <u>\$ 753,716</u> | <u>\$ 748,715</u> | <u>\$ 712,625</u> | \$ 2,215,056          |
| Divide by 3 Years            |                   |                   |                   | 3                     |
| 3 Year Average Debt Service  |                   |                   |                   | \$ 738,352            |

Using the potential 183 new customers that would be served by the Phase 6 construction project, Bullock Pen determined that its requested water rates would produce annual revenues of \$3,381,856.<sup>4</sup> However, if only the 86 customers that have currently applied for service in the Phase 6 construction project area are used, Bullock Pen's requested water rates would produce annual revenues of \$3,335,148, an increase of \$632,596 or 23.4 percent over Staff's normalized revenue from rates of \$2,702,552.

As shown in Table 2 below, Staff's recommended pro forma operations, annual debt service of \$738,352, and the appropriate Debt Service Coverage ("DSC")<sup>5</sup> result in

<sup>4</sup> Id., Exhibit 25, Summary of Proposed Revenue.

<sup>5</sup> A DSC of 1.2x for the Rural Development Bonds and a DSC of 1.1x for the remaining loans and capital leases.

a revenue requirement from rates of \$3,401,034, an increase of \$698,482 or 25.845 percent over Staff's normalized revenue from rates of \$2,702,552.

| Table 2: Staff's Revenue Requirement  |              |   |          |                   |
|---------------------------------------|--------------|---|----------|-------------------|
|                                       | Debt Service |   | Coverage | Requirement       |
| Rural Development                     | \$ 86,467    | x | 0.2      | = \$ 17,293       |
| Loans & Capital Leases                | \$ 651,885   | x | 0.1      | = 65,189          |
| Total Debt Service Coverage           |              |   |          | \$ 82,482         |
| Debt Service - Existing               |              |   |          | 591,761           |
| Debt Service - Phase 6                |              |   |          | 146,591           |
| Add: Pro Forma Operating Expenses     |              |   |          | 2,315,849         |
| Depreciation & Amortization           |              |   |          | 544,416           |
| Taxes Other Than Income               |              |   |          | + 55,196          |
| Total Revenue Requirement             |              |   |          | \$ 3,736,295      |
| Less: Other Income & Deductions       |              |   |          | - 134,756         |
| Revenue Requirement from Operations   |              |   |          | \$ 3,601,539      |
| Less: Other Operating Revenues        |              |   |          | - 200,505         |
| Revenue Requirement from Water Sales  |              |   |          | \$ 3,401,034      |
| Less: Pro Forma Revenue - Water Sales |              |   |          | - 2,702,552       |
| <b>Requested/Recommended Increase</b> |              |   |          | <b>\$ 698,482</b> |
| <b>Percentage Increase</b>            |              |   |          | <b>25.845%</b>    |

Staff finds that Bullock Pen's requested revenue requirement of \$3,335,148 will produce a positive cash flow of \$561,011,<sup>6</sup> and is sufficient for it to pay the pro forma "cash" expenses and meet the debt service requirements of the long-term debt issuances. Therefore, Staff recommends that the Commission allow Bullock Pen to increase its water rates to a level that will generate the requested revenue requirement of \$3,335,148. Should Bullock Pen desire water rates that will generate annual

|  |                   |
|--|-------------------|
| <sup>6</sup> Revenue Requirement - Water Sales | \$ 3,335,148      |
| Add: Other Operating Revenues                  | 200,505           |
| Other Income & Deductions                      | + 134,756         |
| Total Revenue Requirement                      | \$ 3,670,409      |
| Less: Operating Expenses                       | - 2,915,461       |
| Net Operating Income                           | \$ 754,948        |
| Add: Depreciation & Amortization               | + 544,416         |
| Less: Debt Service                             | - 738,352         |
| Net Cash Flow                                  | <u>\$ 561,012</u> |

revenues of \$3,401,034, a level of revenue that Staff finds reasonable, it should amend its application to request the rates set forth in Appendix E and provide documentary evidence to the Commission that it has published notice of those rates pursuant to 807 KAR 5:011, Section 8.

Staff recommends that the Commission approve Bullock Pen's requested water rates, which are set forth in Appendix D. Staff states that the water rates contained in Appendix E will produce the recommended revenue requirement of \$3,401,034.

Bullock Pen requests the Commission to authorize it to increase certain nonrecurring charges to ensure that each nonrecurring charge reflects the actual cost of providing that service.<sup>7</sup> Upon its review of Bullock Pen's cost justification for its nonrecurring charges, Staff finds the proposed charges, as set out in Appendix D, to be reasonable.

Bullock Pen is requesting the Commission to approve its completely revised, comprehensive tariff.<sup>8</sup> Bullock Pen's proposed tariff revisions will be addressed in the final Order in this proceeding.

Bullock Pen also requests the Commission to authorize it to collect a monthly surcharge of \$25 per customer that receives water service in the Phase 6 construction area. Staff has determined that the Phase 6 surcharge should be \$15 per month as calculated in this report and, therefore, recommends that the Commission authorize a Phase 6 surcharge of that amount.

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<sup>7</sup> Application at 9.

<sup>8</sup> Id. at 2.

On October 17, 2005, Bullock Pen entered into a Capital Lease agreement with the Daimler Chrysler Service North America, LLC to purchase a new truck for \$64,371.<sup>9</sup> The capital lease has a five-year term and an interest rate of 4.940 percent per annum.<sup>10</sup>

In response to Staff's inquiry regarding prior Commission authorization of the Capital lease, Bullock Pen states, "It was and is the position of the District that PSC approval for the purchase of a truck such as that evidenced by the Daimler Chrysler financing was not necessary."<sup>11</sup> According to KRS 278.300(1), "No utility shall issue any securities or evidences of indebtedness, or assume any obligation or liability in respect to the securities or evidences of indebtedness of any other person until it has been authorized so to do by order of the commission." Commission approval is not required for debt which is payable in less than two years so long as it is not renewed for a period that exceeds in the aggregate, six years from the issuance date of the original debt.<sup>12</sup>

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<sup>9</sup> Bullock Pen's response to the Commission Staff's Third Information Request, Exhibit 38.

<sup>10</sup> Id.

<sup>11</sup> Id., Item 2(a).

<sup>12</sup> KRS 278.300(8) states, "This section does not apply to notes issued by a utility, for proper purposes and not in violation of law, that are payable at periods of not more than two (2) years from the date thereof, or to like notes, payable at a period of not more than two (2) years from date thereof, that are issued to pay or refund in whole or in part any such notes, or to renewals of such notes from time to time, not exceeding in the aggregate six (6) years from the date of the issue of the original notes so renewed or refunded."



Given that the Capital lease is for a five-year term, it is Staff's belief that Bullock Pen was required to obtain prior Commission authorization. This is not the first instance in which Bullock Pen has violated the provisions of KRS 278.300. In its October 24, 2005 Accounting Inspection Report, Staff noted that Bullock Pen had obtained long-term debt without Commission authorization and advised Bullock Pen that in the future it "should request Commission approval for debt as required by KRS 278.300 or structure the loan so Commission approval is not required."<sup>13</sup> In its response to the Inspection Report, Bullock Pen stated that "the District will have such financing approved by the Public Service Commission."<sup>14</sup>

In another instance in 2005, the KIA, on behalf of 27 water utilities, applied for retroactive authority to issue evidences of indebtedness.<sup>15</sup> Bullock Pen was identified as one of the 27 water utilities that were involved in the KIA refinancing. In that proceeding, the Commission found that "KRS 278.300 makes no provision for the Commission to retroactively approve a utility's issuance of evidences of indebtedness."<sup>16</sup> The Commission also stated:

The Commission places KIA and all of the utilities in question on notice that in the future they will be expected to fully comply with KRS 278.300 and to obtain Commission approval prior to the issuance of any securities or evidences of indebtedness. Their failure to meet their statutory

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<sup>13</sup> Bullock Pen's response to the Commission Staff's Third Information Request, Exhibit 46, "Commissions Staff's Accounting Inspection Report" at 4.

<sup>14</sup> Id., Exhibit 47 at 3.

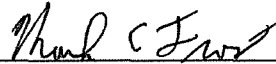
<sup>15</sup> Case No. 2005-00058, Kentucky Infrastructure Authority's Joint Application on Behalf of Certain Water Districts for Authority to Borrow Funds to Refinance Certain Indebtedness to the Kentucky Infrastructure Authority (Ky. PSC Aug. 26, 2005).

<sup>16</sup> Case No. 2005-00058 (Ky. PSC Aug. 26, 2005) at 4.

responsibilities will subject them to administrative sanctions. See KRS 278.990. We furthermore remind all of the water districts and their officers that they alone bear responsibility for obtaining the necessary approvals for the issuance of indebtedness and cannot abdicate their responsibility to another party – even if that party is a state agency.<sup>17</sup>

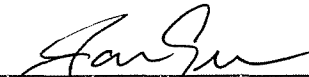
For the aforementioned reasons, Staff recommends that the Commission begin an investigation into Bullock Pen's alleged violation of KRS 278.300. Staff also recommends that the Commission include Bullock Pen's commissioners as parties to the investigation.

Signatures



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Prepared by: Mark C. Frost  
Financial Analyst, Water and Sewer  
Revenue Requirements Branch  
Division of Financial Analysis



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Prepared by: Jason Green  
Rate Analyst, Communications, Water  
and Sewer Rate Design Branch  
Division of Financial Analysis

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<sup>17</sup> Id. at 5.

APPENDIX A  
STAFF REPORT CASE NO. 2008-00170  
BULLOCK PEN'S REQUESTED  
PRO FORMA INCOME STATEMENT

|   | Test-Period<br>Operations | Pro Forma<br>Adjustments | Pro Forma<br>Operations |
|---|---------------------------|--------------------------|-------------------------|
| Operating Revenues:                       |                           |                          |                         |
| Revenues - Unmetered Water Sales          | \$ 4,067                  | \$ 0                     | \$ 4,067                |
| Revenues - Metered Water Sales            | 2,694,094                 | 73,935                   | 2,768,029               |
| Revenues - Sales of Water                 | <u>\$ 2,698,161</u>       | <u>\$ 73,935</u>         | <u>\$ 2,772,096</u>     |
| Other Operating Revenues:                 |                           |                          |                         |
| Forfeited Discounts                       | \$ 60,196                 | \$ 0                     | \$ 60,196               |
| Miscellaneous Service Revenues            | 26,139                    | 0                        | 26,139                  |
| Surcharge Collections - Existing          | 0                         | 0                        | 0                       |
| Surcharge Collections - Phase 6           | 0                         | 0                        | 0                       |
| Total Other Operating Revenues            | <u>\$ 86,335</u>          | <u>\$ 0</u>              | <u>\$ 86,335</u>        |
| Total Operating Revenues                  | <u>\$ 2,784,496</u>       | <u>\$ 73,935</u>         | <u>\$ 2,858,431</u>     |
| Operating Expenses:                       |                           |                          |                         |
| Operation & Maintenance:                  |                           |                          |                         |
| Salaries & Wages - Employees              | \$ 741,478                | \$ 0                     | \$ 741,478              |
| Salaries & Wages - Officers               | 14,000                    | 0                        | 14,000                  |
| Employee Pension & Benefits               | 425,739                   | (76,322)                 | 349,417                 |
| Purchased Water                           | 870,317                   | 0                        | 870,317                 |
| Purchased Power                           | 70,094                    | 0                        | 70,094                  |
| Chemicals                                 | 67,587                    | 0                        | 67,587                  |
| Materials & Supplies                      | 101,680                   | 0                        | 101,680                 |
| Contractual Services - Eng.               | 13,506                    | 0                        | 13,506                  |
| Contractual Services - Accounting         | 38,862                    | 0                        | 38,862                  |
| Contractual Services - Legal              | 17,349                    | 0                        | 17,349                  |
| Contractual Services - Mgt                | 2,679                     | 0                        | 2,679                   |
| Contractual Services - Water Testing      | 20,555                    | 0                        | 20,555                  |
| Contractual Services - Other              | 53,923                    | 0                        | 53,923                  |
| Rental - Building/Real. Prop.             | 4,075                     | 0                        | 4,075                   |
| Rental - Equipment                        | 7,538                     | 0                        | 7,538                   |
| Transportation                            | 46,973                    | 0                        | 46,973                  |
| Insurance                                 | 54,009                    | (13,095)                 | 40,914                  |
| Advertising                               | 167                       | 0                        | 167                     |
| Bad Debt                                  | 9,076                     | 0                        | 9,076                   |
| Miscellaneous                             | 410                       | 0                        | 410                     |
| Total Operation & Maintenance             | <u>\$ 2,560,017</u>       | <u>\$ (89,417)</u>       | <u>\$ 2,470,600</u>     |
| Depreciation                              | 492,160                   | 0                        | 492,160                 |
| Amortization                              | 6,801                     | 0                        | 6,801                   |
| Taxes Other Than Income:                  |                           |                          |                         |
| Public Service Com. Assessment            | 4,611                     | 0                        | 4,611                   |
| Payroll Taxes                             | 54,167                    | 0                        | 54,167                  |
| Utility Operating Expenses                | <u>\$ 3,117,756</u>       | <u>\$ (89,417)</u>       | <u>\$ 3,028,339</u>     |
| Net Utility Operating Income              | <u>\$ (333,260)</u>       | <u>\$ 163,352</u>        | <u>\$ (169,908)</u>     |
| Other Income & Deductions:                |                           |                          |                         |
| Revenues - Merch., Jobbing, Contract Work | 114,174                   | 0                        | 114,174                 |
| Interest Income                           | 20,582                    | 0                        | 20,582                  |
| Total Other Income & Deductions           | <u>\$ 134,756</u>         | <u>\$ 0</u>              | <u>\$ 134,756</u>       |
| Net Income Available for Debt Service     | <u>\$ (198,504)</u>       | <u>\$ 163,352</u>        | <u>\$ (35,152)</u>      |

APPENDIX B  
STAFF REPORT CASE NO. 2008-00170  
STAFF'S RECOMMENDED  
PRO FORMA INCOME STATEMENT

|   | Test-Period<br>Operations | Pro Forma<br>Adjustments | Adj.<br>Ref | Pro Forma<br>Operations |
|---|---------------------------|--------------------------|-------------|-------------------------|
| Operating Revenues:                       |                           |                          |             |                         |
| Revenues - Unmetered Water Sales          | \$ 4,067                  | \$ 0                     |             | \$ 4,067                |
| Revenues - Metered Water Sales            | 2,694,094                 | 8,458                    | (a)         | 2,702,552               |
| Revenues - Sales of Water                 | <u>\$ 2,698,161</u>       | <u>\$ 8,458</u>          |             | <u>\$ 2,706,619</u>     |
| Other Operating Revenues:                 |                           |                          |             |                         |
| Forfeited Discounts                       | \$ 60,196                 | \$ 0                     |             | \$ 60,196               |
| Miscellaneous Service Revenues            | 26,139                    | 0                        |             | 26,139                  |
| Surcharge Collections - Existing          | 0                         | 81,230                   | (b)         | 81,230                  |
| Surcharge Collections - Phase 6           | 0                         | 32,940                   | (c)         | 32,940                  |
| Total Other Operating Revenues            | <u>\$ 86,335</u>          | <u>\$ 114,170</u>        |             | <u>\$ 200,505</u>       |
| Total Operating Revenues                  | <u>\$ 2,784,496</u>       | <u>\$ 122,628</u>        |             | <u>\$ 2,907,124</u>     |
| Operating Expenses:                       |                           |                          |             |                         |
| Operation & Maintenance:                  |                           |                          |             |                         |
| Salaries & Wages - Employees              | \$ 741,478                | \$ (125,391)             | (d)         | \$ 616,087              |
| Salaries & Wages - Officers               | 14,000                    | 0                        |             | 14,000                  |
| Employee Pension & Benefits               | 425,739                   | (100,755)                | (e)         | 324,984                 |
| Purchased Water                           | 870,317                   | 0                        |             | 870,317                 |
| Purchased Power                           | 70,094                    | 0                        |             | 70,094                  |
| Chemicals                                 | 67,587                    | 0                        |             | 67,587                  |
| Materials & Supplies                      | 101,680                   | 0                        |             | 101,680                 |
| Contractual Services - Eng.               | 13,506                    | 0                        |             | 13,506                  |
| Contractual Services - Accounting         | 38,862                    | 0                        |             | 38,862                  |
| Contractual Services - Legal              | 17,349                    | (4,927)                  | (f)         | 12,422                  |
| Contractual Services - Mgt                | 2,679                     | 0                        |             | 2,679                   |
| Contractual Services - Water Testing      | 20,555                    | 0                        |             | 20,555                  |
| Contractual Services - Other              | 53,923                    | 0                        |             | 53,923                  |
| Rental - Building/Real. Prop.             | 4,075                     | 0                        |             | 4,075                   |
| Rental - Equipment                        | 7,538                     | 0                        |             | 7,538                   |
| Transportation                            | 46,973                    | 0                        |             | 46,973                  |
| Insurance                                 | 54,009                    | (13,095)                 | (g)         | 40,914                  |
| Advertising                               | 167                       | 0                        |             | 167                     |
| Bad Debt                                  | 9,076                     | 0                        |             | 9,076                   |
| Miscellaneous                             | 410                       | 0                        |             | 410                     |
| Total Operation & Maintenance             | <u>\$ 2,560,017</u>       | <u>\$ (244,168)</u>      |             | <u>\$ 2,315,849</u>     |
| Depreciation                              | 492,160                   | 45,455                   | (h)         | 537,615                 |
| Amortization                              | 6,801                     | 0                        |             | 6,801                   |
| Taxes Other Than Income:                  |                           |                          |             |                         |
| Public Service Com. Assessment            | 4,611                     | 0                        |             | 4,611                   |
| Payroll Taxes                             | 54,167                    | (3,582)                  | (i)         | 50,585                  |
| Utility Operating Expenses                | <u>\$ 3,117,756</u>       | <u>\$ (202,295)</u>      |             | <u>\$ 2,915,461</u>     |
| Net Utility Operating Income              | <u>\$ (333,260)</u>       | <u>\$ 324,922</u>        |             | <u>\$ (8,338)</u>       |
| Other Income & Deductions:                |                           |                          |             |                         |
| Revenues - Merch., Jobbing, Contract Work | 114,174                   | 0                        |             | 114,174                 |
| Interest Income                           | 20,582                    | 0                        |             | 20,582                  |
| Total Other Income & Deductions           | <u>\$ 134,756</u>         | <u>\$ 0</u>              |             | <u>\$ 134,756</u>       |
| Net Income Available for Debt Service     | <u>\$ (198,504)</u>       | <u>\$ 324,922</u>        |             | <u>\$ 126,418</u>       |

APPENDIX C  
STAFF REPORT CASE NO. 2008-00170  
STAFF'S PRO FORMA ADJUSTMENTS

a. Metered Water Sales. Bullock Pen proposes to increase its test-period revenue from metered water sales of \$2,694,094 by \$71,935 to reflect the 183 new customers that were projected to be added to the system when the Phase 6 construction project is completed.<sup>1</sup> However, as of August 5, 2009, only 86 residents had signed up for water service in the Phase 6 project area.<sup>2</sup> Applying the current tariffed rates to Bullock Pen's billing analysis and using only the 86 new Project 6 customers, Staff determined that the pro forma operating revenue from water sales should be increased by \$8,458 to a pro forma level of \$2,702,552.

b. Existing Surcharges. Bullock Pen currently has four construction surcharges listed in its tariff. In its August 27, 2009 filing, Bullock Pen provided the current number of customers in each construction surcharge area as of July 31, 2009. Using the current number of customers in each surcharge area and the tariffed surcharges, Staff calculates annual collections from existing surcharges of \$81,230 as shown in Table 1 below. Accordingly, Staff recommends that operating revenues be increased by that amount.

| Table 1: Existing Surcharges    |                      |                      |                       |           |  |
|---------------------------------|----------------------|----------------------|-----------------------|-----------|--|
|                                 | Monthly<br>Surcharge | Current<br>Customers | Surcharge Collections |           |  |
|                                 |                      |                      | Monthly               | Annual    |  |
| Phase 5 Surcharge               | \$ 10.00             | 259                  | \$ 3,108              | \$ 31,080 |  |
| Phase 7 Surcharge               | \$ 12.52             | 53                   | \$ 636                | 7,963     |  |
| Phase 8 Surcharge               | \$ 11.46             | 202                  | \$ 2,424              | 27,779    |  |
| Phase 10 Surcharge              | \$ 10.72             | 112                  | \$ 1,344              | 14,408    |  |
| Pro Forma Surcharge Collections |                      |                      |                       | \$ 81,230 |  |

<sup>1</sup> Bullock Pen's response to the Commission Staff's Second Information Request, Item 3(a), Exhibit 24, Projected Revenue from Customers Added by Phase 6 Construction.

<sup>2</sup> Bullock Pen's response to the Commission Staff's Third Information Request, Item 1(a).

c. Phase 6 Construction Surcharge. Originally, Bullock Pen used an estimated customer count of 180 to show that the Phase 6 construction project would support a surcharge of \$33.75 per month.<sup>3</sup> In its February 18, 2009 filing, Bullock Pen updated its Phase 6 surcharge calculations to reflect that 80 customers had actually signed up, which resulted in a revised surcharge of \$50.88 per month.<sup>4</sup> However, Bullock Pen requests that, in lieu of the surcharges that it can justify, the Commission authorize the predetermined maximum surcharge of \$25.00 per month.<sup>5</sup>

Staff agrees with the Commission's previous assessment in that "the most appropriate means to recover the cost of a water main extension project is through the general rates."<sup>6</sup> However, the Commission has previously authorized four construction surcharges that allow Bullock Pen to recover the financing cost of line extension projects from those customers who benefit from the project.<sup>7</sup> Staff opines that Bullock

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<sup>3</sup> Application, Exhibit 6, Preliminary Engineering Report, Phase 6 - Surcharge Estimate (Preliminary).

<sup>4</sup> Final Engineering Report, Phase 6 Surcharge Estimate.

<sup>5</sup> Id.

<sup>6</sup> Case No. 2005-00231, Application of the Bullock Pen Water District for a Certificate of Public Convenience and Necessity to Construct and Finance Improvement Projects and to Implement Surcharges to its Existing Rates Pursuant to KRS 278.020 and 278.300 (Ky. PSC Dec. 12, 2005) at 4.

<sup>7</sup> See, e.g., Case No. 2002-00015, Application of the Bullock Pen Water District for a Certificate of Public Convenience and Necessity to Construct and Finance an Improvements Project and to Implement a Surcharge to Its Existing Rates Pursuant To KRS 278.020 and 278.300 (Ky. PSC Mar. 18, 2002); Case No. 2004-00339, Application of the Bullock Pen Water District for a Certificate of Public Convenience and Necessity to Construct and Finance an Improvements Project and to Implement a Surcharge to Its Existing Rates Pursuant to KRS 278.020 and 278.300 (Ky. PSC Feb. 14, 2005); Case No. 2005-00231 (Ky. PSC Dec. 12, 2005).

Pen has adequately demonstrated that a construction surcharge for the Phase 6 construction project is reasonable.

Bullock Pen conducted a “drive-by” count of the potential customers that could be served in the Phase 6 construction project area.<sup>8</sup> This drive-by count indicated that there were 183 potential customers, but, as of August 1, 2009, only 86 residents had signed up for water service.<sup>9</sup> Bullock Pen states that the historical trend is that, after construction begins in a project area, a significant number of additional sign-ups will occur.<sup>10</sup> According to Bullock Pen, this trend should occur in the Phase 6 project area.<sup>11</sup> For this reason Staff is using the 183 potential customers to ensure that in the future Bullock Pen will not collect an amount greater than intended.

When developing the level of surcharges in those prior cases, the Commission considered the additional revenues that will be generated as a result of the new customers. Using estimated financial information, Bullock Pen determined that each new customer that will be served by the Phase 6 construction project will generate additional net operating income of approximately \$48.<sup>12</sup> In Case No. 2005-00231, the Commission determined that Bullock Pen’s net operating income per customer was \$100.65 based upon the operating revenues and expenses reported for the calendar

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<sup>8</sup> Bullock Pen’s Response to the Commission Staff Third Information Request, Item 1(a).

<sup>9</sup> Id.

<sup>10</sup> Id.

<sup>11</sup> Id.

<sup>12</sup> February 18, 2009, Supplemental Information Filing, Final Engineering Report, Phase 6 Surcharge Estimate.

year ended December 31, 2004.<sup>13</sup> Using the pro forma operating revenues and expenses contained in this report, Staff determined that the net operating income per customer is \$70.<sup>14</sup>

Assuming that each of the potential 183 customers that will receive water service from the Phase 6 construction project will generate an additional annual net operating income of \$70, Staff has determined that the Phase 6 project surcharge should be \$15 per month, as shown in Table 2 below. Accordingly, Staff recommends Bullock Pen's operating revenues be increased by \$32,940,<sup>15</sup> the annual surcharge collections.

|  |    |         |
|--|----|---------|
| Project Costs - Kenton County Customers Only     | \$ | 863,511 |
| Less: Tap-on Fees                                | -  | 183,000 |
| Total Loan to Serve Kenton County Customers Only | \$ | 680,511 |
| Annual Interest Rate                             |    | 3.0%    |
| Term   |    | 20      |
| Annual Debt Service                              | \$ | 45,741  |
| Operating Income Per Customer                    | \$ | 70.00   |
| Multiplied by: Phase 6 - Kenton County Customers | x  | 183     |
| Operating Income per Kenton County Cust.         | \$ | 12,810  |
| Total Annual Debt Service - Phase 6 Project      | \$ | 45,741  |
| Less: Operating Income per Kenton County Cust.   | -  | 12,810  |
| Annual Debt Service - Phase 6 Surcharge          | \$ | 32,931  |
| Divided by: No. Kenton County Customers          | ÷  | 183     |
| Annual Surcharge per Customer                    | \$ | 180     |
| Divided by: 12 Months                            | ÷  | 12      |
| Monthly Surcharge - Phase 6 Project              | \$ | 15      |

<sup>13</sup> Case No. 2005-00231, Order of Dec. 12, 2005, at 5.

|  |    |         |
|--|----|---------|
| <sup>14</sup> Annual Debt Service & Coverage | \$ | 820,834 |
| Less: Annual Debt Service - Phase 6 Project  |    | 45,741  |
| Existing Surcharge Collections               |    | 81,230  |
| Non-operating Income                         |    | 134,756 |
| Other Operating Revenues                     | -  | 86,335  |
| Net Operating Income - Water Rates           | \$ | 472,772 |
| Divided by: Total Customers                  | ÷  | 6,781   |
| Net Operating Income per Customer ≈          | \$ | 70.00   |

<sup>15</sup> \$15 (Phase 6 Surcharge) x 183 (Customers) x 12 (Months) = \$32,940.



d. Salaries and Wages - Employees. Bullock Pen reports a test-period level of salaries and wages - employees expense of \$741,478. Using Bullock Pen's current staff level and the hourly wages that became effective on July 1, 2008, Staff calculates a pro forma salaries and wages expense of \$616,087, as shown in Table 3 below. Accordingly, Staff recommends salaries and wages expense - employees be decreased by \$125,391 to reflect its pro forma level of \$616,087.

| Employee Position | Hours Worked |          |        | Pro Forma Rates as of 7/01/08 |          | Pro Forma Salaries & Wages |
|-------------------|--------------|----------|--------|-------------------------------|----------|----------------------------|
|                   | Regular      | Overtime | % Cap  | Reg.                          | Over.    |                            |
| Distribution      | 2,080.0      | 204.0    | 3.11%  | \$ 23.29                      | \$ 34.94 | \$ 53,842                  |
| Clerical          | 2,080.0      | 7.0      | 0.00%  | \$ 13.22                      | \$ 19.83 | 27,637                     |
| Clerical          | 2,080.0      | 6.5      | 1.65%  | \$ 16.07                      | \$ 24.11 | 33,027                     |
| Distribution      | 2,080.0      | 72.5     | 12.61% | \$ 24.89                      | \$ 37.34 | 47,611                     |
| Clerical          | 2,080.0      | 0.0      | 0.00%  | \$ 10.00                      | \$ 15.00 | 20,800                     |
| Clerical          | 2,080.0      | 15.5     | 1.59%  | \$ 18.52                      | \$ 27.78 | 38,334                     |
| Distribution      | 2,080.0      | 78.5     | 0.00%  | \$ 14.45                      | \$ 21.68 | 31,758                     |
| Operator          | 2,080.0      | 61.5     | 0.00%  | \$ 20.00                      | \$ 30.00 | 43,445                     |
| Distribution      | 2,080.0      | 64.5     | 9.09%  | \$ 18.06                      | \$ 27.09 | 35,740                     |
| Asst Office Mgr   | 2,080.0      | 10.0     | 0.00%  | \$ 63,866.43                  | N/A      | 63,866                     |
| Distribution      | 2,080.0      | 45.0     | 0.00%  | \$ 14.75                      | \$ 22.13 | 31,676                     |
| Clerical          | 2,080.0      | 0.0      | 0.00%  | \$ 10.00                      | \$ 15.00 | 20,800                     |
| Distribution      | 2,080.0      | 49.0     | 0.00%  | \$ 23.03                      | \$ 34.55 | 49,595                     |
| Distribution      | 2,080.0      | 42.5     | 0.00%  | \$ 10.00                      | \$ 15.00 | 21,438                     |
| Office Manager    | 2,080.0      | 0.0      | 0.00%  | \$ -                          | N/A      | 0                          |
| Operator          | 2,080.0      | 67.5     | 0.00%  | \$ 13.49                      | \$ 20.24 | 29,425                     |
| Asst Dist Mgr     | 2,080.0      | 0.0      | 4.08%  | \$ 69,948.93                  | N/A      | 67,093                     |
| District Manager  | 2,080.0      | 0.0      | 0.00%  | \$ -                          | N/A      | 0                          |
| <b>Total</b>      |              |          |        |                               |          | <b>\$ 616,087</b>          |

e. Employee Pensions and Benefits. Bullock Pen reports a test-period level of employee pensions and benefits expense of \$425,739. On July 1, 2009, the County Employees Retirement System employer contribution rate was increased to 16.16 percent.<sup>16</sup> Using the current employee health insurance premiums and the employer

<sup>16</sup> Bullock Pen's Response to the Commission Staff's Second Information Request, Exhibit 33.

retirement contribution rate of 16.16 percent, Staff calculates a pro forma level of employee pensions and benefits expense of \$324,984. Staff recommends that Bullock Pen's employee pensions and benefits expense be decreased by \$100,755 to reflect Staff's pro forma level.

f. Contractual Services - Legal. Bullock Pen reports a test-period level of contractual services - legal expense of \$17,349. In reviewing the invoices from Bullock Pen's attorney, Thomas R. Nienaber, Staff determined that \$4,927 of the legal fees were either for nonrecurring or capital projects. For this reason, Staff is reducing contractual services - legal expense by \$4,927 to eliminate those test-period legal fees from test-period operating expenses.

g. Insurance. Bullock Pen proposes to reduce its test-period insurance expense of \$54,009<sup>17</sup> by \$13,095 for a pro forma level of \$40,914. "In September 2008, Bullock Pen advertised for bids from insurance carriers for the upcoming insurance coverage period."<sup>18</sup> As a result of this bidding process, Bullock Pen awarded the insurance contract to the Chas Bilz Agency.<sup>19</sup> Bullock Pen's proposed adjustment reflects the insurance premiums that became affective in 2009.

Staff opines that an adjustment to reflect the 2009 insurance premiums meets the rate-making criteria of being known and measurable. Accordingly, Staff

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<sup>17</sup> \$10,073 (Automobile) + \$16,321 (Liability) + \$6,739 (Other) + \$20,876 (Workers Compensation) = \$54,009.

<sup>18</sup> Bullock Pen's Response to the Commission Staff's Second Information Request, Item 16.

<sup>19</sup> Id.

recommends that the Commission accept Bullock Pen's proposed adjustment to reduce insurance expense by \$13,095.

h. Depreciation. Bullock Pen reports a test-period level of depreciation expense of \$492,160. Staff recommends that depreciation expense be increased by \$45,455 to reflect depreciating the cost to construct the Project 6 line extension over a 50-year depreciation life.

i. Payroll Taxes. Bullock Pen reports a test-period payroll tax expense of \$54,167. Using the pro forma payroll determined reasonable herein and the current "FICA" rate of 7.65 percent, Staff calculates a pro forma payroll tax expense of \$50,585, a decrease of \$3,582 below the reported level. Accordingly, Staff proposes to decrease payroll tax expense by \$3,582.

APPENDIX D  
 STAFF REPORT CASE NO. 2008-00170  
 RATES AND CHARGES  
 BULLOCK PEN REQUESTED

**RATES AND CHARGES**

5/8" x 3/4" Meter:

|          |        |         |          |                   |
|----------|--------|---------|----------|-------------------|
| First    | 2,000  | gallons | \$ 23.75 | Minimum bill      |
| Next     | 3,000  | gallons | \$ 6.92  | per 1,000 gallons |
| Next     | 5,000  | gallons | \$ 6.45  | per 1,000 gallons |
| Next     | 10,000 | gallons | \$ 6.32  | per 1,000 gallons |
| All Over | 20,000 | gallons | \$ 5.55  | per 1,000 gallons |

1" Meter:

|          |        |         |          |                   |
|----------|--------|---------|----------|-------------------|
| First    | 5,000  | gallons | \$ 44.51 | Minimum bill      |
| Next     | 5,000  | gallons | \$ 6.45  | per 1,000 gallons |
| Next     | 10,000 | gallons | \$ 6.32  | per 1,000 gallons |
| All Over | 20,000 | gallons | \$ 5.55  | per 1,000 gallons |

1 1/2" Meter:

|          |        |         |          |                   |
|----------|--------|---------|----------|-------------------|
| First    | 10,000 | gallons | \$ 76.76 | Minimum bill      |
| Next     | 10,000 | gallons | \$ 6.32  | per 1,000 gallons |
| All Over | 20,000 | gallons | \$ 5.55  | per 1,000 gallons |

2" Meter:

|          |        |         |           |                   |
|----------|--------|---------|-----------|-------------------|
| First    | 20,000 | gallons | \$ 139.96 | Minimum bill      |
| All Over | 20,000 | gallons | \$ 5.55   | per 1,000 gallons |

Bulk Loading Station \$ 6.17 per 1,000 gallons

Phase 6 Surcharge \$ 15.00<sup>1</sup>

**NONRECURRING CHARGES**

|                              |             |
|------------------------------|-------------|
| Meter Reread                 | \$ 35.00    |
| Meter Test                   | \$ 50.00    |
| Reconnection                 | \$ 50.00    |
| Service Call - Investigation | \$ 35.00    |
| Meter Relocation             | Actual Cost |

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<sup>1</sup> Bullock Pen proposed a surcharge of \$25.00 per month to be charged to those customers receiving service in the Phase 6 construction project area. In this report, Staff has determined that the Phase 6 surcharge should be \$15.00 per month.

APPENDIX E  
 STAFF REPORT CASE NO. 2008-00170  
 RATES AND CHARGES  
 BULLOCK PEN COULD JUSTIFY

**RATES AND CHARGES**

5/8" x 3/4" Meter:

|          |        |         |          |                   |
|----------|--------|---------|----------|-------------------|
| First    | 2,000  | gallons | \$ 26.59 | Minimum bill      |
| Next     | 3,000  | gallons | \$ 8.80  | per 1,000 gallons |
| Next     | 5,000  | gallons | \$ 7.96  | per 1,000 gallons |
| Next     | 10,000 | gallons | \$ 7.11  | per 1,000 gallons |
| All Over | 20,000 | gallons | \$ 6.26  | per 1,000 gallons |

1" Meter:

|          |        |         |          |                   |
|----------|--------|---------|----------|-------------------|
| First    | 5,000  | gallons | \$ 52.99 | Minimum bill      |
| Next     | 5,000  | gallons | \$ 7.96  | per 1,000 gallons |
| Next     | 10,000 | gallons | \$ 7.11  | per 1,000 gallons |
| All Over | 20,000 | gallons | \$ 6.26  | per 1,000 gallons |

1 1/2" Meter:

|          |        |         |          |                   |
|----------|--------|---------|----------|-------------------|
| First    | 10,000 | gallons | \$ 92.79 | Minimum bill      |
| Next     | 10,000 | gallons | \$ 7.11  | per 1,000 gallons |
| All Over | 20,000 | gallons | \$ 6.26  | per 1,000 gallons |

2" Meter:

|          |        |         |           |                   |
|----------|--------|---------|-----------|-------------------|
| First    | 20,000 | gallons | \$ 163.89 | Minimum bill      |
| All Over | 20,000 | gallons | \$ 6.26   | per 1,000 gallons |

Bulk Loading Station \$ 6.98 per 1,000 gallons

Phase 6 Surcharge \$ 15.00

**NONRECURRING CHARGES**

|                              |             |
|------------------------------|-------------|
| Meter Reread                 | \$ 35.00    |
| Meter Test                   | \$ 50.00    |
| Reconnection                 | \$ 50.00    |
| Service Call - Investigation | \$ 35.00    |
| Meter Relocation             | Actual Cost |

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