

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF CANNONSBURG WATER)
DISTRICT FOR (1) APPROVAL OF EMERGENCY)
RATE RELIEF AND (2) APPROVAL OF THE) CASE NO. 2011-00217
INCREASE IN NONRECURRING CHARGES)

ORDER

Pursuant to 807 KAR 5:001, Section 10, Cannonsburg Water District ("Cannonsburg District"), has applied to adjust its rates for water service. By this Order, the Commission establishes rates that will produce additional annual revenues of \$242,725, or an 11.02 percent increase over normalized test-period revenues from water sales of \$2,201,936. For a residential customer who consumes 5,000 gallons of water monthly, his or her monthly bill will increase from \$38.35 to \$41.88, or approximately 9.2 percent. The Commission also authorizes the assessment of a monthly surcharge of \$5.53 on all customers for a period of 36 months to fund Cannonsburg District's non-revenue water reduction efforts.

Cannonsburg District, a water district organized pursuant to KRS Chapter 74, owns and operates facilities that distribute water to approximately 3,733 customers in Boyd and Greenup counties, Kentucky.¹ Its last general rate adjustment occurred in August 2004.²

¹ *Annual Report of Cannonsburg Water District to the Public Service Commission for the Calendar Year Ended December 31, 2010* ("Annual Report") at 5, 27.

² Case No. 2004-00159, *Application of Cannonsburg Water District for Approval of the Proposed Increase in Rates for Water Service* (Ky. PSC Aug. 18, 2004).

On August 8, 2011, Cannonsburg District applied for an adjustment of its rates for water service.³ Using its historical operations for the calendar year ended December 31, 2010 and adjusting for known and measureable changes, Cannonsburg District proposed rates that would produce additional revenues from water sales of \$183,330 and total annual revenues of \$2,234,187.⁴ The proposed rates would increase the monthly bill of a customer who uses 5,000 gallons of water from \$36.00 to \$39.50, or approximately 9.72 percent.⁵

Cannonsburg District moved for leave to place its proposed rates into effect prior to the end of the suspension period due to its financial condition.⁶ On February 27, 2011, after a hearing on this motion and finding that Cannonsburg District “failed to demonstrate that the immediate implementation of the proposed rates is necessary to avoid material impairment to its credit or operations,” we denied Cannonsburg District’s motion.

On February 27, 2012, we also released a Commission Staff report on the proposed rate adjustment and Cannonsburg District’s operations during the test period. In this report, Commission Staff found that “Cannonsburg [District]’s proposed rates will

³ Cannonsburg District tendered its application with the Commission on June 27, 2011. Upon review of the application, the Executive Director found that the application did not comply with 807 KAR 5:001 and did not accept it for filing purposes. On July 25, 2011, Cannonsburg District supplemented its application to cure the noted deficiencies and requested a deviation from 807 KAR 5:001, Section 10(6)(b). It renewed and supplemented its request for a deviation on August 8, 2011. On August 10, 2011, the Commission granted Cannonsburg District’s request for a deviation, accepted the application for filing, and directed that it be considered filed as of August 8, 2011.

⁴ Application at 3.

⁵ These rates do not reflect adjustments in Cannonsburg District’s rates due to increases in its cost of purchased water.

⁶ Following the hearing on its motion, Cannonsburg District requested authority to assess a “surcharge whose proceeds are restricted to addressing non-revenue water reduction efforts.” Letter from Danny Clarkson, Manager, Cannonsburg Water District, to Gerald Wuetcher, Commission Staff Counsel (Aug. 18, 2011).

produce a level of revenue that is insufficient to meet the water district's reasonable operating expenses and service its existing debt."⁷ It further found that, based upon Cannonsburg District's test-period operations, Cannonsburg District required total revenues of \$2,549,230 to meet its reasonable operating expenses, to service its existing debt, and provide for equity growth and, to reach this level of revenue, required a rate adjustment to generate additional annual revenue of \$242,725 over normalized revenue from rates of \$2,201,936.⁸ Commission Staff also recommended that, in addition to an adjustment of rates for general service, a surcharge to finance Cannonsburg District's efforts to reduce its non-revenue water be authorized.⁹

In our Order releasing the Commission Staff report, we directed Cannonsburg District to submit comments on Commission Staff's findings and recommendations and to specifically address Commission Staff's findings regarding the water district's revenue requirement and the need for a surcharge to finance non-revenue water reduction efforts. We further directed that, if Cannonsburg District wished to revise its request for rate adjustment to reflect Commission Staff's findings, it should publish notice of its revised request in a newspaper of general circulation in its service area.

On March 5, 2012, Cannonsburg District advised the Commission that it accepted the findings and recommendations contained in the Commission Staff report

⁷ Mark Frost and Sam Reid, *Commission Staff Report on Cannonsburg Water District* (released Feb. 27, 2012) at 7.

⁸ *Id.*

⁹ In its report, Commission Staff did not address Cannonsburg District's proposed revisions to several nonrecurring charges.

and would publish the required notice to inform its ratepayers of its decision to revise its rate request.¹⁰

Having considered the evidence of record and being otherwise sufficiently advised, the Commission finds that:

1. Except where they conflict with the findings contained in this Order, the findings contained in Commission Staff's report are supported by the evidence of record, are reasonable, and should be adopted as the Commission's own findings.

2. The calendar year ending December 31, 2010 should be used as the test period to determine the reasonableness of Cannonsburg District's existing and proposed rates.

3. Based upon pro forma test-period operations, Cannonsburg District's pro forma annual revenue is \$2,306,865.¹¹ Approximately \$2,201,936 of this revenue results from water sales.

¹⁰ In its response, Cannonsburg District also advised the Commission that it was now requiring its employees to pay 25 percent of their health insurance premiums and, in conjunction with the Kentucky Rural Water Association, was preparing a comprehensive non-revenue water plan for submission to the Commission. It also noted Commission Staff's failure to make any findings or recommendations regarding its proposed revisions to several nonrecurring charges.

¹¹ \$2,201,936 (Revenue from Metered Water Sales) + \$88,193 (Other Operating Revenue) + \$16,736 (Interest Income) = \$2,306,865. Other Operating Revenue includes forfeited discounts and miscellaneous service revenue

4. Based upon pro forma test-period operations, Cannonsburg District's pro forma total operating expenses, after adjusting for known and measurable changes, are \$2,227,481.¹²

5. As of December 31, 2010, Cannonsburg District had outstanding long-term debt of \$422,021.¹³ Given Cannonsburg District's relatively small amount of outstanding debt, the use of an operating ratio¹⁴ to determine Cannonsburg District's revenue requirement is more appropriate than the debt service coverage methodology.¹⁵

6. An operating ratio of 0.88 will permit Cannonsburg District to meet its reasonable operating expenses, service its existing debt, and provide for equity growth, and should be used to determine Cannonsburg District's total revenue requirement.

¹² This amount does not include \$233,625 in purchased water expenses that Cannonsburg District incurred during the test period. During the test period, Cannonsburg District experienced unaccounted-for water loss of 29.91 percent. "Unaccounted-for water loss" equals the difference of the total amount of water produced and purchased and the sum of water sold, water used for fire protection purposes, and water used in treatment and distribution operations (e.g., backwashing filters, line flushing). 807 KAR 5:066, Section 6(3), provides that "for rate making purposes, a utility's unaccounted-for water loss shall not exceed fifteen (15) percent of the total water produced and purchased, excluding water used by a utility in its own operations." For the calculation of Cannonsburg District's unaccounted-for water loss, see *Commission Staff Report on Cannonsburg Water District*, Attach. D at 3.

The Commission notes that in its report Commission Staff recommended two different amounts regarding unaccounted-for water loss. At page 4 of its Report, Commission Staff recommended exclusion of \$233,625 of the cost of lost water from rate recovery. At page 8, it recommended a reduction of \$221,348 in purchased water expenses to comply with 807 KAR 5:066, Section 6(3). Based upon our review of the Report, we conclude that Commission Staff intended to recommend a reduction of \$233,625 and that the record fully supports such reduction.

¹³ *Annual Report* at 23.

¹⁴ Operating Ratio is defined as the ratio of expenses, including depreciation and taxes, to gross revenues. It is illustrated by the following equation:

$$\text{Operating Ratio} = \frac{\text{Operating Expenses} + \text{Depreciation} + \text{Taxes}}{\text{Gross Revenues}}$$

¹⁵ See, e.g., Case No. 8468, *An Adjustment of the Rates of Plantation Hill Sewage Treatment Plant, Inc.* (Ky. PSC Jun. 25, 1982); 1 A.J.G. Priest, *Principals of Public Utility Regulation* (Michie 1969) 220-224.

7. Applying an operating ratio of 0.88 to Cannonsburg District's pro forma operating expenses of \$2,227,481, and including a dollar-for-dollar coverage of interest expense, produces a total revenue requirement of \$2,549,230.¹⁶ After considering Cannonsburg District's interest income and miscellaneous operating income, Cannonsburg District requires \$2,444,661 of revenue from water sales, or \$242,725 more than its current rates produce.

8. Cannonsburg District's proposed rates will produce a level of revenue that is insufficient to meet the water district's reasonable operating expenses and to service its debt.¹⁷

9. The rates set forth in the Appendix to this Order will produce total annual revenues of \$2,549,230 and revenues from water sales of \$2,444,661, will allow Cannonsburg District to meet its reasonable operating expenses and debt service requirements, and will provide for equity growth.

10. The rates set forth in the Appendix to this Order are fair, just, and reasonable and should be assessed for service that Cannonsburg District renders on and after the date of this Order.

11. During the test period, Cannonsburg District's unaccounted-for water loss was 161,946,746 gallons, or 29.91 percent.

¹⁶ $\$2,227,481$ (Pro Forma Operating Expenses) \div $0.88 = \$2,531,228$. $\$2,531,228 + \$18,002$ (Three-Year Average Interest Expense) = $\$2,549,230$.

¹⁷ Cannonsburg District's proposed rates fail to reflect the increased cost of purchased water due to increases that its suppliers implemented after the filing of Cannonsburg District's application for rate adjustment.

12. During the period from 2002 through 2010, unaccounted-for water losses represented approximately 31.31 percent¹⁸ of Cannonsburg District's water purchases.

13. Cannonsburg District's pro forma purchased water expense has been reduced by \$221,348 for ratemaking purposes to comply with 807 KAR 5:066, Section 6(3).

14. The unaccounted-for water loss expense reduction will severely restrict Cannonsburg District's cash flow, will limit the funds available to Cannonsburg District to address its non-revenue water problem, and will impair Cannonsburg District's ability to take the necessary action to focus on its leak detection and repair.

15. The use of a monthly surcharge assessed over a 36-month period is a reasonable means of funding Cannonsburg District's unaccounted-for water loss reduction efforts.

16. The total proceeds produced by such surcharge should be based upon that amount of expenses that 807 KAR 5:066, Section 6(3), requires to be disallowed.

17. Cannonsburg District should be permitted to assess a surcharge to fund its unaccounted-for water loss reduction efforts subject to the following conditions:

a. Within 90 days of the entry of a Final Order, Cannonsburg District should file with the Commission a comprehensive unaccounted-for water loss reduction

¹⁸ $1,241,131,000$ (Total Unaccounted-For Water Loss 2002-2010) \div $3,963,683,000$ (Total Water Purchases 2002-2010) = 31.31%.

plan¹⁹ that identifies the sources of unaccounted-for water loss and the amount of water loss from each source, establishes priorities and a time schedule for eliminating each source of unaccounted-for water loss, and provides a detailed spending plan for the proceeds of a surcharge.

b. Cannonsburg District should deposit surcharge collections in a separate interest-bearing account.

c. No surcharge proceeds should be withdrawn from the separate interest-bearing account until the Commission has approved Cannonsburg District's comprehensive unaccounted-for water loss plan.

d. Cannonsburg District should file monthly activity reports with the Commission that include a statement of monthly surcharge billings and collections; a monthly surcharge bank statement; a list of each payment from the account, its payee and a description of its purpose; and invoices supporting each payment.

e. Cannonsburg District must file monthly water-loss reports with the Commission.

f. Surcharge proceeds should not be used to reimburse Cannonsburg District for unaccounted-for water loss reduction expenses incurred prior to the issuance of a Final Order in this proceeding.

¹⁹ In its report, Commission Staff recommended that Cannonsburg District be required to develop a comprehensive non-revenue water reduction plan. "Non-revenue water" is defined as "those components of system input volume that are not billed and produce no revenue; equal to unbilled authorized consumption plus apparent losses plus real losses." American Water Works Association, *Water Audits and Loss Control Programs* (3d ed. 2009) at 271. As it is not limited to unaccounted for water loss, Commission Staff's recommendation involves a plan of a much wider scope than that required by this Order. We encourage, but will not require, Cannonsburg District to develop such a plan.

g. Cannonsburg District's failure to comply with any conditions attached to its assessment of the surcharge should result in termination of the surcharge and the refund of all surcharge proceeds previously collected.

18. Cannonsburg District should, subject to the conditions set forth in finding paragraph 17, be authorized to assess a monthly surcharge of \$5.53 to each customer for a period of 36 months or until \$700,875 has been assessed, whichever occurs first.

19. Cannonsburg District's proposed revisions to its nonrecurring charges will not result in rates that exceed the specific cost of the activity in question.

IT IS THEREFORE ORDERED that:

1. Except when they contradict or conflict with the findings contained in this Order, the findings contained in Commission Staff's report are adopted and incorporated by reference into this Order as if fully set out herein.

2. Cannonsburg District's proposed rates are denied.

3. The rates set forth in the Appendix to this Order are approved for water service that Cannonsburg District renders on and after the date of this Order.

4. Subject to the conditions set forth in ordering paragraphs 5 through 13, Cannonsburg District is authorized to assess a monthly surcharge of \$5.53 on each customer beginning on June 1, 2012 and continuing for a period of 36 months or until the total amount of the surcharge assessed equals \$700,875, whichever occurs first. Cannonsburg District's failure to comply with the conditions set forth in ordering paragraphs 5 through 13 shall result in termination of the surcharge and the refund of all collected surcharge proceeds.

5. Within 90 days of the entry of a Final Order, Cannonsburg District shall file with the Commission a comprehensive unaccounted-for water loss reduction plan that identifies the sources of unaccounted-for water loss and the amount of lost water from each source, establishes priorities and a time schedule for eliminating each source of unaccounted-for water, and provides a detailed spending plan for the proceeds of the surcharge.

6. Cannonsburg District shall deposit surcharge collections in a separate interest-bearing account.

7. Cannonsburg District shall not withdraw any surcharge proceeds from the separate interest-bearing account prior to the Commission's approval of Cannonsburg District's comprehensive unaccounted-for water loss reduction plan.

8. On the fifteenth day of each month for 36 months from the date of this Order or until all surcharge proceeds are expended, Cannonsburg District shall file with the Commission a monthly activity report that includes a statement of monthly surcharge billings and collections; a monthly surcharge bank statement; a list of each payment from the account, its payee and a description of its purpose; and invoices supporting each payment.

9. On the fifteenth day of each month for 36 months from the date of this Order or until all surcharge proceeds are expended, Cannonsburg must file a monthly water-loss report with the Commission.²⁰

10. Cannonsburg District shall not use any surcharge proceeds for reimbursement of unaccounted-for water loss reduction expenses incurred prior to the issuance of a Final Order in this proceeding.

²⁰ The report format is found at <http://psc.ky.gov/agencies/psc/forms/wateruse.xls>.

11. Cannonsburg District shall consider all surcharge collections as contributions and shall account for them in the manner that the Uniform System of Accounts for Class A and B Water Districts and Associations prescribes.

12. Cannonsburg District shall debit monthly billings of the surcharge to customer accounts receivable and credit the contribution account.

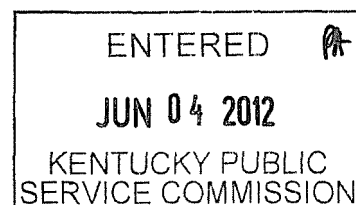
13. When Cannonsburg District collects the surcharge from the customer, it shall debit special funds and credit the customer account.

14. Within 20 days of the date of this Order, Cannonsburg District shall file revised tariff sheets with the Commission setting forth the rates approved in this Order.

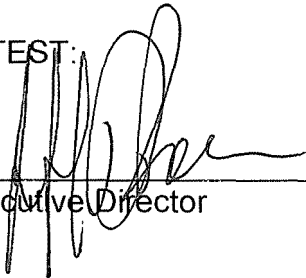
15. Any documents filed in the future pursuant to this Order shall reference this case number and shall be retained in the utility's general correspondence file.

16. The Executive Director is authorized to grant reasonable extensions of time for the filing of any documents required by this Order upon Cannonsburg District's showing of good cause for such extension.

By the Commission



ATTEST:



Executive Director

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2011-00217 DATED JUN 04 2012

The following rates and charges are prescribed for the customers in the area served by Cannonsburg Water District. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of the Commission prior to the effective date of this Order.

Monthly Water Rates

5/8 x 3/4-Inch Meter

First	2,000 gallons	\$ 19.50	Minimum Bill
Next	3,000 gallons	7.46	per 1,000 gallons
Next	15,000 gallons	7.05	per 1,000 gallons
Next	30,000 gallons	6.63	per 1,000 gallons
Next	50,000 gallons	6.23	per 1,000 gallons
Over	100,000 gallons	5.79	per 1,000 gallons

1 1/2-Inch Meter

First	5,000 gallons	\$ 41.88	Minimum Bill
Next	15,000 gallons	7.05	per 1,000 gallons
Next	30,000 gallons	6.63	per 1,000 gallons
Next	50,000 gallons	6.23	per 1,000 gallons
Over	100,000 gallons	5.79	per 1,000 gallons

2-Inch and 3-Inch Meters

First	20,000 gallons	\$ 147.63	Minimum Bill
Next	30,000 gallons	6.63	per 1,000 gallons
Next	50,000 gallons	6.23	per 1,000 gallons
Over	100,000 gallons	5.79	per 1,000 gallons

6-Inch Meter

First	50,000 gallons	\$ 346.53	Minimum Bill
Next	50,000 gallons	6.23	per 1,000 gallons
Over	100,000 gallons	5.79	per 1,000 gallons

12-Inch Meter

First	100,000 gallons	\$ 658.03	Minimum Bill
Over	100,000 gallons	5.79	per 1,000 gallons

Wholesale volumetric rate

Big Sandy Water District	\$	3.67	per 1,000 gallons
City of Greenup	\$	3.67	per 1,000 gallons

Leak Adjustment Rate	\$	3.67	per 1,000 gallons
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Non-Revenue Water Reduction Surcharge

A surcharge of \$5.53 shall be assessed monthly to each customer for the period from June 1, 2012 until May 31, 2015, or until the total amount of the surcharge assessed equals \$700,875, whichever occurs first. Assessment of this surcharge is subject to the conditions set forth in this Order.

Nonrecurring Charges

Connection/Turn On	\$	40
Connection/Turn On After Hours	\$	75
Meter Reread Charge	\$	40
Re-Connection	\$	40
Re-Connection After Hours	\$	75
Service Call/Investigation	\$	40
Service Call/Investigation After Hours	\$	75
Damage to Lid or Meter Equipment		Actual Cost

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