

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF MUHLENBERG COUNTY)
WATER DISTRICT NO. 3 FOR RATE)
ADJUSTMENT FOR SMALL UTILITIES) CASE NO. 2012-00017
PURSUANT TO 807 KAR 5:076)

ORDER

Pursuant to 807 KAR 5:076, Muhlenberg County Water District No. 3 ("Muhlenberg District") applied for an adjustment of rates for water service. By this Order, the Commission establishes rates that will produce additional annual revenues of \$98,338, or a 10.80 percent increase over normalized test-period revenues from water sales of \$910,826. These rates will increase the monthly bill of a customer who consumes 5,000 gallons of water monthly from \$25.04 to \$27.75, or approximately 10.82 percent.

Muhlenberg District, a water district organized pursuant to KRS Chapter 74, owns and operates facilities that distribute water to approximately 2,151 customers in Muhlenberg and McLean counties, Kentucky.¹

¹ *Annual Report of Muhlenberg County Water District No. 3 to the Public Service Commission for the Calendar Year Ended December 31, 2010 ("Annual Report")* at 5 and 27.

On January 24, 2012, Muhlenberg District filed with the Commission its application for an adjustment of its rates for water service.² Using its historical operations for the calendar year ending December 31, 2010, and adjusting for known and measureable changes, Muhlenberg District proposed rates that would produce additional revenues from water sales of \$118,114, an increase of 12.98 percent over normalized revenues from water sales of \$910,826.

On March 30, 2012, Commission Staff issued a report of its findings and recommendations regarding the proposed rate adjustment and Muhlenberg District's operations during the test year. It found that Muhlenberg District's pro forma operating expenses were \$921,700.³ Using an operating ratio methodology to determine Muhlenberg District's total revenue requirement, it recommended that the water district should be permitted rates that would produce total revenues from water sales of \$1,009,164.

On April 23, 2012, Muhlenberg District advised the Commission in writing that it accepted the findings and recommendations of the report and that the matter should be submitted to the Commission for decision based upon the existing record. Pursuant to the terms of the Commission's Order of February 23, 2012, this case stood submitted for decision upon receipt of Muhlenberg District's written notice.

² Muhlenberg District elected to file its application using electronic filing procedures. It submitted its application electronically on January 12, 2012. Pursuant to 807 KAR 076, Section 5, the application is deemed filed upon the date of electronic submission if the original and one paper copy are filed with the Commission within two business days of the date of electronic submission. Muhlenberg District did not submit the original and paper copy until January 24, 2012. Accordingly, the date of submission of the original and paper copy was deemed the date of filing.

³ Commission Staff has provided conflicting recommendations regarding the level of Muhlenberg District's pro forma operating expenses. At page 3 of the Report, Commission Staff finds pro forma operating expenses of \$920,224. At Appendix A of the Report, however, it reports pro forma operating expenses of \$921,700. At Appendix C of the Report, Commission Staff used the latter amount to calculate Muhlenberg District's total revenue requirements.

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 the Order, the findings contained in Commission Staff's report are supported by the evidence of record, are reasonable and should be adopted.

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

3. Based upon pro forma test-period operations, Muhlenberg District's pro forma annual revenue from Water Sales, Other Operating Revenue and Other Income, is \$949,126.⁴ Approximately \$910,826 of this revenue is from water sales.

4. Based upon pro forma test-period operations, Muhlenberg District's pro forma total operating expenses, after adjusting for known and measurable changes, are \$921,700.⁵

⁴ \$910,826 (Operating Revenues-Water Sales) + \$24,696 (Other Operating Revenues) + \$13,604 (Interest Income) = \$949,126. Other Operating Revenue includes forfeited discounts and miscellaneous service revenue.

⁵ This amount does not include \$20,606 in purchased water expenses that Muhlenberg District incurred during the test period. During the test period, Muhlenberg District experienced unaccounted-for water loss of 19.225 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." We have also excluded \$889 of purchased power expenses to eliminate the purchased power expense associated with the cost of pumping excess water loss.

In addition to the elimination of expenses associated with excessive unaccounted-for water loss, the Commission also reduced Muhlenberg District's proposed pro forma salary and wages expense by \$18,000 to correct for an error in the calculation of the expense. Total operating expenses includes an increase of \$13,979 over the test-period salary and wages expense.

5. Muhlenberg District has no outstanding long-term debt.⁶

6. Since Muhlenberg District has no outstanding long-term debt, the use of an operating ratio⁷ is the most appropriate methodology to determine Muhlenberg District's revenue requirement.⁸

7. An operating ratio of 88 percent will permit Muhlenberg District to meet its reasonable operating expenses and provide for a reasonable operating margin and should be used to determine Muhlenberg District's total revenue requirement.

8. Applying an operating ratio of 88 percent to Muhlenberg District's pro forma operating expenses of \$921,700 and taking into consideration test-period interest payments on customer deposits of \$77, Muhlenberg District has a total revenue requirement of \$1,047,463.⁹

9. Based upon normalized test-period sales, Muhlenberg District's proposed rates will produce total annual revenues from water sales of \$1,028,940. When other test-period sources of revenues are considered, Muhlenberg District's proposed rates will produce total annual revenues of \$1,067,240.¹⁰

⁶ *Annual Report* at 22-24.

⁷ Operating Ratio is defined as the ratio of expenses, including depreciation and taxes, to gross revenues. It is illustrated by the following equation:

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

⁸ See, e.g., Case No. 8468, *An Adjustment of the Rates of Plantation Hill Sewage Treatment Plant, Inc.* (Ky. PSC June 25, 1982); 1 A.J.G Priest, *Principles of Public Utility Regulation* (Michie 1969) 220-224.

⁹ \$921,700 (Pro Forma Operating Expenses) ÷ 0.88 = \$1,047,386. \$1,047,386 + \$77 (Interest Expense) = \$1,047,463 (Total Revenue Requirement)

¹⁰ \$1,028,940 (Operating Revenues-Water Sales) + \$24,696 (Other Operating Revenues) + \$13,604 (Interest Income) = \$1,067,240.

10. Muhlenberg District's proposed rates will produce revenues in excess of Muhlenberg District's total revenue requirement and are unreasonable.

11. Based upon normalized test-period water sales, the rates set forth in the Appendix to this Order will produce total annual revenues from water sales of \$1,009,164 and result in total annual revenues of \$1,047,463.¹¹

12. In the absence of any cost-of-service study, the most reasonable means of allocating Muhlenberg District's increased costs among Muhlenberg District ratepayers is by increasing Muhlenberg District's current rates by an equal percentage derived from the percentage increase in revenue requirement over adjusted test-period revenues. The rates set forth in the Appendix to this Order are consistent with this methodology.

13. The rates set forth in the Appendix to this Order are fair, just, and reasonable and should be approved for service rendered on and after the date of this Order.

IT IS THEREFORE ORDERED that:

1. Except where 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.

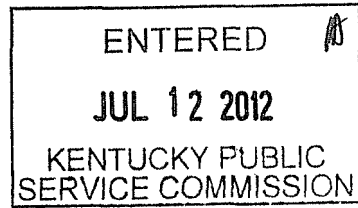
2. Muhlenberg District's proposed rates are denied.

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

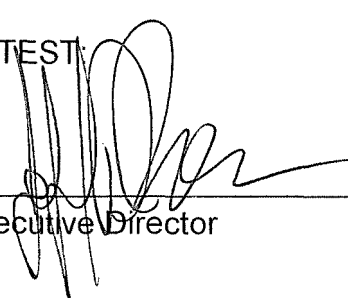
¹¹ \$1,009,164 (Operating Revenues-Water Sales) + \$13,604 (Interest Income) + \$24,696 (Other Operating Revenue) = 1,047,463 (Total Revenue Requirement).

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

By the Commission



ATTEST



Executive Director

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2012-00017 DATED JUL 12 2012

The following rates and charges are prescribed for the customers in the area served by Muhlenberg County Water District No. 3. 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

First	2,000 gallons	\$15.21 Minimum Bill
Next	8,000 gallons	4.18 per 1,000 gallons
Next	10,000 gallons	3.89 per 1,000 gallons
Next	30,000 gallons	3.52 per 1,000 gallons
Over	50,000 gallons	3.24 per 1,000 gallons

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