COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF ADAIR COUNTY)	
WATER DISTRICT FOR AN ALTERNATIVE RATE)	CASE NO.
ADJUSTMENT)	2021-00315

ORDER

On September 2, 2021, Adair County Water District (Adair District) filed an application with the Commission, pursuant to 807 KAR 5:076, requesting to adjust its rates for water service. This application was filed pursuant to the Commission's Order in Case No. 2020-00308.¹ In its application, Adair District requested rates that would increase annual water sales revenues by \$216,705, or a 5.34 percent increase to proforma present rate water sales revenues.

To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated September 23, 2021, which, among other things, required the Commission Staff to file a report containing its findings regarding Adair District's application. Pursuant to the September 23, 2021 Order, on December 16, 2021, Commission Staff issued a report (Staff Report) summarizing its findings regarding Adair District's requested rate adjustment. In the Staff Report, Commission Staff found that Adair District's adjusted test-year operations support an overall revenue requirement of

¹ Case No. 2020-00308, Electronic Application of the Adair County Water District for a Certificate of Public Convenience and Necessity to Construct a System Improvements Project and an Order Approving a Change in Rates and Authorizing the Issuance of Securities Pursuant to KRS 278.023 (filed May 14, 2020) at 9, ordering paragraph 16.

\$5,398,095 and that an annual revenue increase of \$1,193,636, or 29.44 percent, is necessary to generate the overall revenue requirement.²

On December 28, 2021, Adair District filed with the Commission its comments on the Staff Report. In its response, Adair District did not agree with Commission Staff's removal of certain labor expenses from nonrecurring charges, but did not wish to contest the adjustments in this case. Adair District also disagreed with Commission Staff's reduction of employee health and dental insurance expenses stating that Commission Staff did not consider the value of the total compensation package, labor market conditions, or the level of benefits generally provided to employees in the utility sector or among Kentucky's water utilities, but, like with the nonrecurring charges, chose not to contest these adjustments. Adair District did note that the rates contained in the Staff Report are higher than the application because Commission Staff did not phase-in the depreciation into the revenue calculations, as proposed in the application. Adair District argued that the utility has operated well without the working capital deprecation would provide and that the utility would still have ample working capital. Adair District voiced its concern about the impact the rate increase will have on its customer base, citing the lower than median state household income in Adair District's service territory, and requested that the Commission phase-in the proposed rates over a three-year period. Provided that the recommended water service rates are accepted as filed, Adair District did not request that a conference or hearing be held.³

² Staff Report at 18. Note that the amount listed on page 4 under Summary of Findings incorrectly listed the increase as \$1,199.636.

³ Adair District's Response to Staff Report (filed Dec. 28, 2021).

LEGAL STANDARD

Alternative rate adjustment proceedings, such as this one, are governed by 807 KAR 5:076, which establishes a simplified process for small utilities to use to request rate adjustments, with the process designed to be less costly to the utility and to the utility ratepayers. The Commission's standard of review of a utility's request for a rate increase is well established. In accordance with KRS 278.030 and case law, Adair District is allowed to charge its customers "only 'fair, just and reasonable rates." Further, Adair District bears the burden of proof to show that the proposed rate increase is just and reasonable, under KRS 278.190(3).

WATER LOSS

Pursuant to 807 KAR 5:066, Section (6)3, water loss is limited to 15 percent for ratemaking purposes. As noted in the Staff Report, Adair District's test-year water loss was 13.08 percent. Accordingly, at a 13.08 percent water loss, the annual cost to Adair District is \$39,128.⁵

BACKGROUND

Adair District is a water district organized pursuant to KRS Chapter 74. It owns and operates a water distribution system through which it provides water service to approximately 7,556 residential customers, and 395 commercial customers in Adair County, Kentucky.⁶ Adair District both produces and purchases its water from Jamestown

⁴ City of Covington v. Public Service Commission, 313 S.W.2d 391 (Ky. 1958); and Pub. Serv. Comm'n v. Com. of Kentucky v. Dewit Water District, 720 S.W.2d 725 (Ky. 1986).

⁵ Staff Report at 2.

⁶ Annual Report of Adair District to the Public Service Commission for the Calendar Year Ended December 31, 2020 (Annual Report) at 12 and 49.

Utilities and the city of Campbellsville. Adair District has never filed a general rate case; rather rate adjustments have occurred through 023 financing cases.⁷

The Commission would note that, pursuant to the filings in this case, Adair District has been doing business as "Columbia/ Adair Utilities District aka Adair County Water District," yet has filed no notice of this name change with the Commission. The Commission finds that Adair District shall file updated tariff sheets that reflect this change in name and provide written notice to the Executive Director of the Commission of the name change.

TEST PERIOD

The calendar year ended December 31, 2020, was used as the test year to determine the reasonableness of Adair District's existing and proposed water rates as required by 807 KAR 5:076, Section 9.

SUMMARY OF REVENUE AND EXPENSES

The Staff Report summarizes Adair District's pro forma income statement as follows:

	2020	Rate Study	Pro Forma
	Annual Report	Adjustments	Operations
Total Operating Revenues	\$ 3,847,952	\$ 333,457	\$4,181,409
Utility Operating Expenses	3,869,610	(214,532)	3,655,078
Net Utility Operating Income	(21,658)	547,989	526,331
Total Utility Operating Income	\$ (21,658)	\$547,989	\$ 526,331

⁷ A 023 loan is when the applicant requests Commission approval of federal funding pursuant to KRS 278.023(3). Here the application must be approved within 30 days and the Commission cannot reject the application.

MODIFICATIONS TO STAFF'S FINDINGS

Adair District proposed adjustments to revenues and expenses to reflect current and expected operating conditions. In the Staff Report, Commission Staff proposed additional adjustments. The Commission accepts the findings contained in the Staff Report. These adjustments are discussed below.

<u>Billing Analysis Adjustment</u>. In the Staff Report, Commission Staff recommended to accept Adair District's proposed adjustment to increase test year revenues by \$271,583⁸ to reflect the normalization of sales revenues of due to an increase in rates approved in Case No. 2020-00308. The Commission finds that this adjustment is a known and measurable change to Total Metered Sales, is reasonable, and should be accepted.

Miscellaneous Service Revenues - Late Payment Fees. In the Staff Report, Commission Staff recommended an increase to Adair District's test-year Miscellaneous Service Revenues of \$80,3379 to reflect the normalization of Late Payment Fees to account for the moratorium regarding the collection of late payment fees from March through December 2020 due to the COVID-19 pandemic. The Commission finds that this adjustment, which is the average of the past three-year's late payment fees, is a known and measurable change to Miscellaneous Service Revenues, is reasonable, and should be accepted.

⁸ Staff Report at 8, Adjustment A.

⁹ Staff Report at 8 and 9, Adjustment B.

Miscellaneous Service Revenues - Nonrecurring Charges. In the Staff Report, Commission Staff discussed Adair District's Nonrecurring Charges¹⁰ in which estimated labor costs, previously included in determining the amount of Nonrecurring Charges, are removed. In its response to the Staff Report, Adair District stated that it did not agree with the removal of certain nonrecurring charge labor expenses, but did not wish to contest the adjustments in this case.¹¹ Commission Staff recommended a reduction to Adair District's test-year Miscellaneous Service Revenues of \$18,463¹² to reflect the change in the nonrecurring charges. The Commission finds that this adjustment is a known and measurable change to Miscellaneous Service Revenues, is reasonable, and should be accepted.

<u>Salaries and Wages - Employees</u>. In the Staff Report, Commission Staff recommended an increase to Adair District's test-year Salaries and Wages - Employees of \$22,434¹³ to reflect an increase in employee's salaries and wages, and the change in the number of full-time employees subsequent to the test year. In addition, the adjustment reflected the alteration to Adair District's hourly employee's allocation between the water and wastewater divisions. The Commission finds that this adjustment is a known and measurable change to Other Water Revenues, is reasonable, and should be accepted.

<u>Expenses Related to Meter Installation.</u> In the Staff Report, Commission Staff recommended a decrease to Adair District's Salaries and Wages - Employees expense

¹⁰ *Id.* at 5 and 6.

¹¹ Adair District's Response to Staff Report (filed Dec. 28, 2021).

¹² Staff Report, at 9, Adjustment C.

¹³ Id., at 9 and 10, Adjustment D.

by \$24,750 and Materials and Supplies by \$57,750¹⁴ for the expenses related to the installation of 121 new water connections. The Commission finds that this adjustment is a known and measurable change to Materials and Supplies, is reasonable, and should be accepted.

<u>Salaries and Wages - Officers.</u> In the Staff Report, Commission Staff recommended a decrease to Adair District's Salaries and Wages - Officers expense by \$10,392¹⁵ to reflect the change to Adair District's water to wastewater division allocation percentages. The Commission finds that this adjustment is a known and measurable change to Materials and Supplies, is reasonable, and should be accepted.

Employee Pensions and Benefits- Retirement Contribution. In the Staff Report, Commission Staff recommended a decrease to Adair District's Employee Pensions and Benefits - Retirement Contribution of \$152,565.¹⁶ The decrease is the summation of an increase to retirement contributions due to an increase in contribution percentage from 24.06 percent to 26.95 percent and the decrease in employee's salaries and wages. The Commission finds that these adjustments are known and measurable changes to Employee Pensions and Benefits and Interest Expense, are reasonable, and should be accepted.

Employee Pensions and Benefits - Insurance Premiums. In the Staff Report, Commission Staff recommended a decrease to Adair District's Employee Pensions and Benefits of \$38,761¹⁷ to reflect the adjustment of Single Health Insurance premiums paid

¹⁴ *Id.*, at 10 and 11, Adjustment E.

¹⁵ Id. at 11–12, Adjustment F.

¹⁶ *Id.* at 13, Adjustment G.

¹⁷ *Id.* at 13–15, Adjustment H.

by Adair District from 100 percent to 78 percent, Family Health insurance premiums from 100 percent to 66 percent, and Dental and Vision Insurance from 100 percent to 60 percent. The Commission finds that this adjustment is a known and measurable change to Employee Pensions and Benefits, is reasonable, and should be accepted.

Depreciation Expense. In the Staff Report, Commission Staff recommended a decrease to Adair District's test-year Depreciation Expense of \$39,307¹⁸ to reflect the adjustment of the useful life of capital assets to the midpoint of the National Association of Regulatory Utility Commissioners depreciation study. Commission Staff's adjustment does not include the proposed phase-in for Depreciation Expense over a three-year period. The Commission reject's Adair District's proposed phase-in of depreciation as this does not follow general ratemaking principles and finds that Commission Staff's proposed adjustment is a known and measurable change to Depreciation Expense, is reasonable, and should be accepted. However, as discussed below, although the Commission does include the Staff Report's recommended level of Depreciation Expense, it nonetheless orders a phase-in of Adair District's revenue requirement later in this Order.

<u>Capitalization of Test-Year Water Taps</u>. In the Staff Report, Commission Staff recommended an increase to Adair District's test-year Depreciation Expense of \$1,941¹⁹ to reflect the capitalization of the materials and supplies associated with the installation

¹⁸ *Id.* at 15–16.

¹⁹ *Id.* at 16–17, Adjustment I.

of new water connections. The Commission finds that this adjustment is a known and measurable change to Depreciation Expense, is reasonable, and should be accepted.

<u>Taxes other than Income</u>. In the Staff Report, Commission Staff recommended an increase to Adair District's test-year Taxes other than Income Expense of \$63,834²⁰ to reflect an increase to payroll taxes due to an increase to salaries and wages, as well as the inclusion of the PSC Assessment Fee when compared to the reported test-year Taxes other Than Income. The Commission finds that this adjustment is a known and measurable change to Taxes other than Income, is reasonable, and should be accepted.

Based on the commission's findings discussed above, the following table summarizes Adair District's adjusted pro forma operations:²¹

	Staff Report Pro Forma	Commission Adjustments	Final Pro Forma
Total Operating Revenues Utility Operating Expenses	\$ 4,181,409 3,655,078	\$ - -	\$4,181,409 3,655,078
Net Utility Operating Income	526,331		526,331
Total Utility Operating Income	\$ 526,331	\$ -	\$ 526,331

REVENUE REQUIREMENTS

Based upon the Commission's findings and determinations herein, Adair District requires an increase in revenues of \$1,193,636, or 29.44 percent above pro forma present rate revenues as shown below:

²⁰ Id. at 17, Adjustment J.

²¹ See Appendix A for a complete pro forma.

Pro Forma Operating Expenses	\$ 3,655,078
Plus: Avg. Annual Principal and Interest Payments	1,452,514
Debt Coverage Requirement	290,503
	5 000 005
Overall Revenue Requirement	5,398,095
Less: Other Operating Revenue	(126,278)
Miscellaneous Service Revenue	-
Interest Income	(23,050)
Revenue Required From Water Sales	5,248,767
Revenue from Sales at Present Rates	\$ (4,055,131)
Required Revenue Increase	1,193,636
Percentage Increase	29.44%

RATE DESIGN

Adair District proposed an across-the-board 5.34 percent increase to its monthly water rates. Adair District applied this across-the-board increase as no cost of service study (COSS) was performed. Adair District stated that a COSS was not completed as there had not been any material change in the water system to warrant a COSS.²² The Commission finds that in the absence of a COSS, the proposed across-the-board method is an appropriate and equitable method to allocate the increased cost to Adair District's customers. Based upon the revenue requirement of \$5,248,767, or a 29.44 percent increase, this would result in an increase of \$11.69 for a typical residential customer's monthly water bill.²³

Adair District expressed its concern about a 29.44 percent increase in the average monthly bill in its response to the Staff Report. The Commission recognizes and shares

 $^{^{22}}$ Adair District's Response to Commission Staff's First Request for Information (filed Oct. 20, 2021), Item 10.b.

²³ Staff Report at 5.

Adair District's concerns regarding the impact of such an increase. However, the Commission also recognizes and stresses the importance of financial integrity and notes that depreciation reserves should be maintained as a funding source for cost recovery and recurring replacement of a utility's investment.24 The Commission has allowed utilities to phase-in large rate increases as long as the revenues generated in each phase meet the debt service requirements and expenses and eventually fully fund depreciation.²⁵ The record contains no evidence that permitting Adair District to temporarily assess water rates at a level lower than could be supported will result in any degradation or reduction in the quality of service that Adair District currently provides, particularly given the eventual and relatively near-term increase provided for herein. Due to the absence of evidence that the quality of Adair District's service will decline or be degraded as a result of a temporary lower level of revenue than otherwise justifiable, and in recognition of the balance required by the provision of service under KRS 278.030(2) and the impact an increase of this magnitude would have on customers, the Commission finds that a six-year phase-in of rates should be approved. Based upon the revenue requirement of \$5,248,767 determined herein, a phase-in of approximately 9.81 percent the first year, followed by two annual increases of approximately 8.93 percent and 8.20 percent, respectively, will result in sufficient revenues for the provision of service on an

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²⁴ See Case No. 2019-00041, *Electronic Investigation into Excessive Water Loss by Kentucky's Jurisdictional Water Utilities* (Ky. PSC July 30, 2021).

²⁵ See Case No. 2021-00094, Electronic Application of Garrison-Quincy-Ky-O-Heights Water District for a Rate Adjustment Pursuant to 807 KAR 5:076 (Ky. PSC Nov. 24, 2021).

on-going basis. The following table illustrates the impact of the average monthly residential bill:²⁶

	Average Bill	Difference	% Difference
Current	\$39.71		
Phase 1	\$43.61	\$3.90	9.83%
Phase 2	\$47.52	\$3.90	8.95%
Phase 3	\$51.40	\$3.88	8.18%

SUMMARY

After consideration of the evidence of record and being otherwise sufficiently advised, the Commission finds that:

- 1. The recommendations contained in the Staff Report are supported by the evidence of record and are reasonable and should be adopted.
- 2. The Commission has historically used a Debt Service Coverage (DSC) method to calculate the revenue requirement for water districts or associations with outstanding long-term debt. Application of the Commission's DSC method to Adair District's pro forma operations results in an Overall Revenue Requirement of \$5,398,095. A revenue increase of \$1,193,636 from water service rates is necessary to generate the overall revenue requirement.
- 3. The water service rates proposed by Adair District would produce inadequate revenues and should be denied.
- 4. Phase 1, Phase 2, and Phase 3 water service rates set forth in Appendix B are fair, just and reasonable and should be approved

IT IS THEREFORE ORDERED that:

²⁶ The typical residential customers uses approximately 3,830 gallons per month.

- 1. The findings contained in the Staff Report are adopted and incorporated by reference into this Order as if fully set out herein.
 - 2. The water service rates proposed by Adair District are denied.
- 3. The Phase 1 water rates set forth in Appendix B to this Order are approved for services rendered by Adair District on and after the date of this Order.
- 4. The Phase 2 water rates set forth in Appendix B to this Order are approved for services rendered by Adair District on and after one year of the date of this Order.
- 5. The Phase 3 water rates set forth in Appendix B to this Order are approved for services rendered by Adair District on and after two years of the date of this Order.
- 6. One week prior to the effective date of Phase 2, and one week prior to the effective date of the Phase 3 water rates, Adair District shall publish notice following the requirements of 807 KAR 5:076, Section 5. The customer notice shall contain only the rate comparison being implemented for that rate phase.
- 7. Within 45 days of publishing the notice required in ordering paragraph number 6, Adair District shall file proof of notice as required pursuant to 807 KAR 5:076, Section 5(3).
- 8. Within 20 days of the date of entry of this Order, Adair District shall file with this Commission, using the Commission's electronic Tariff Filing System, new tariff sheets reflecting the current name by which Adair District is doing business, setting forth the rates and charges approved herein and their effective date, and stating that the rates and charges were authorized by this Order.

- 9. Within 20 days of the date of entry of this Order, Adair District shall provide written notice to the Executive Director of the Commission of the change in utility name and current name by which Adair District is doing business.
 - 10. This case is closed and removed from the Commission's docket.

By the Commission

ENTERED

FEB 10 2022

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KENTUCKY PUBLIC
SERVICE COMMISSION

ATTEST:

Executive Director

inda G. Britwell

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2021-00315 DATED FEB 10 2022

	Test Year	Staff Report Adjustment	Commission Adjustments	Final Pro Forma
Operating Revenues Total Metered Sales	\$3,783,548	271,583		\$ 4,055,131
Other Water Revenues Miscellaneous Service Revenues	64,404	80,337		400.070
Rents from Water Property Other Water Revenues		(18,463)		126,278
Total Operating Revenues	\$ 3,847,952	333,457		\$4,181,409
Operating Expenses Operation and Maintenance Expenses				
Salaries and Wages - Employees	624,947	22,434 (24,750)		622,631
Salaries and Wages - Officers Employee Pensions and Benefits	119,495 546,306	10,392 (152,565)		129,887
Purchased Water		(38,761)		354,980
Purchased Power Chemicals	196,280 178,360	()		196,280 178,360
Materials and Supplies Contractual Services	211,829 10,875	(57,750)		154,079 10,875
Water Testing Transportation Expenses Insurance	15,014 26,766 71,663			15,014 26,766 71,663
Bad Debt Miscellaneous Expense	23,307 399,872			23,307 399,872
Total Operation and Maintenance Expenses	2,424,714	(241,000)		2,183,714
Depreciation	1,444,896	(39,307) 1,941		1,407,530
Amortization Taxes Other Than Income Income Tax Expense		63,834		63,834
Utility Operating Expenses	3,869,610	(214,532)		3,655,078
Utility Operating Income	(21,658)	547,989		526,331
Income Available to Service Debt	(21,658)	547,989		526,331

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2021-00315 DATED FEB 10 2022

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

Monthly Water Rates Phase 1

5/8- x 3/4-Inch Meter First 1,000 Gallons Next 4,000 Gallons Next 5,000 Gallons Next 15,000 Gallons Over 25,000 Gallons	\$\$\$\$\$	0.00686 0.00571	Minimum Bill Per Gallon Per Gallon Per Gallon Per Gallon
1-Inch Meter First 5,000 Gallons Next 5,000 Gallons Next 15,000 Gallons Over 25,000 Gallons	\$ \$ \$ \$	0.00571	Minimum Bill Per Gallon Per Gallon Per Gallon
1 1/2-Inch Meter First 10,000 Gallons Next 15,000 Gallons Over 25,000 Gallons	\$ \$ \$		Minimum Bill Per Gallon Per Gallon
2-Inch Meter First 16,000 Gallons Next 9,000 Gallons Over 25,000 Gallons	\$ \$ \$		Minimum Bill Per Gallon Per Gallon
Wholesale Rate City of Edmonton Green Taylor Water District East Casey Water District	\$ \$ \$	0.00275	Per Gallon Per Gallon Per Gallon

Monthly Water Rates Phase 2 – Effective One Year from the date of this Order

5/8- x 3/4-Inch Meter First 1,000 Gallons Next 4,000 Gallons Next 5,000 Gallons Next 15,000 Gallons Over 25,000 Gallons	\$ \$ \$ \$ \$	0.00747 0.00622	Minimum Bill Per Gallon Per Gallon Per Gallon Per Gallon	
1-Inch Meter First 5,000 Gallons Next 5,000 Gallons Next 15,000 Gallons Over 25,000 Gallons	\$ \$ \$	0.00622	Minimum Bill Per Gallon Per Gallon Per Gallon	
1 1/2-Inch Meter First 10,000 Gallons Next 15,000 Gallons Over 25,000 Gallons	\$ \$ \$		Minimum Bill Per Gallon Per Gallon	
2-Inch Meter First 16,000 Gallons Next 9,000 Gallons Over 25,000 Gallons	\$ \$ \$		Minimum Bill Per Gallon Per Gallon	
Wholesale Rate City of Edmonton Green Taylor Water District East Casey Water District	\$ \$ \$	0.00300	Per Gallon Per Gallon Per Gallon	
Monthly Water Rates Phase 3 – Effective Two Years from the date of this Order				
5/8- x 3/4-Inch Meter First 1,000 Gallons Next 4,000 Gallons Next 5,000 Gallons Next 15,000 Gallons Over 25,000 Gallons	\$ \$ \$ \$	0.00809 0.00673	Minimum Bill Per Gallon Per Gallon Per Gallon Per Gallon	
1-Inch Meter First 5,000 Gallons Next 5,000 Gallons Next 15,000 Gallons Over 25,000 Gallons	\$ \$ \$	0.00673	Minimum Bill Per Gallon Per Gallon Per Gallon	

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1 1/2-Inch Meter First 10,000 Gallons Next 15,000 Gallons Over 25,000 Gallons	\$ \$ \$		Minimum Bill Per Gallon Per Gallon
2-Inch Meter First 16,000 Gallons Next 9,000 Gallons Over 25,000 Gallons	\$ \$ \$		Minimum Bill Per Gallon Per Gallon
Wholesale Rate City of Edmonton Green Taylor Water District East Casey Water District	\$ \$ \$	0.00324	Per Gallon Per Gallon Per Gallon

Nonrecurring Charges

Connection/Turn-On Charge	\$ 12.88
Connection/Turn-On Charge (After Hours)	\$ 30.98
Meter Re-read Charge	\$ 12.88
Meter Re-read Charge (After Hours)	\$ 30.98
Meter Test Charge	\$ 12.88
Reconnection Charge	\$ 12.88
Reconnection Charge (After Hours)	\$ 30.98
Return Check Charge	\$ 6.60
Service Call/ Investigation Charge	\$ 12.88
Service Call/ Investigation Charge (After Hours)	\$ 30.98
Meter Reading Re-Check Charge	\$ 12.88
Meter Reading Re-Check Charge (After Hours)	\$ 30.98

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