

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF NORTH)	CASE NO.
MANCHESTER WATER ASSOCIATION, INC.)	2023-00183
FOR AN ALTERNATIVE RATE ADJUSTMENT)	

NOTICE OF FILING OF COMMISSION STAFF'S REPORT

Notice is hereby given that, in accordance with the Commission's Order of July 31, 2023, as amended by Orders entered September 12, 2023, October 6, 2023, and January 5, 2024, the attached report containing the recommendations of Commission Staff regarding the Applicant's proposed rate adjustment has been filed in the record of the above-styled proceeding. Pursuant to the Commission's July 31, 2023 Order, North Manchester Water Association, Inc. (North Manchester Water) is required to file written comments regarding the recommendations of Commission Staff no later than 14 days from the date of service of this report. The Commission directs North Manchester Water to the Commission's July 22, 2021 Order in Case No. 2020-00085¹ regarding filings with the Commission.



Linda C. Bridwell, PE
Executive Director
Public Service Commission
P.O. Box 615
Frankfort, KY 40602

DATED JAN 11 2024

cc: Parties of Record

¹ Case No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19* (Ky. PSC July 22, 2021), Order (in which the Commission ordered that for case filings made on and after March 16, 2020, filers are NOT required to file the original physical copies of the filings required by 807 KAR 5:001, Section 8).

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COMMISSION STAFF'S REPORT
ON NORTH MANCHESTER WATER ASSOCIATION, INC.

North Manchester Water Association, Inc. (North Manchester Water) is a water utility organized pursuant to KRS Chapter 273 that owns and operates a distribution system through which it provides retail water service to approximately 1,942 residential customers, 16 commercial customers, 2 industrial customers, and 8 public authorities that reside in Clay County, Kentucky.¹

On July 6, 2023,² North Manchester Water filed its application with the Commission requesting an adjustment to its water service rates pursuant to 807 KAR 5:076. To comply with the requirements of 807 KAR 5:076, Section 9,³ North Manchester Water used the calendar year ended December 31, 2022, as the basis for its application.⁴ The

¹ *Annual Report of North Manchester Water to the Public Service Commission for the Calendar Year Ended December 31, 2022* (2022 Annual Report) at 12 and 49.

² North Manchester Water tendered its application on June 1, 2023. By letter dated June 12, 2023, the Commission rejected the application for filing deficiencies. The deficiencies were subsequently cured, and the application is deemed filed on July 6, 2023.

³ 807 KAR 5:076, Section 9 states that the reasonableness of the proposed rates shall be determined using a 12-month historical test period, adjusted for known and measurable changes, that coincides with the reporting period of the applicant's annual report for the immediate past year.

⁴ Application, Item 9.

application was filed pursuant to the Commission's Order in Case No. 2021-00339,⁵ which required North Manchester Water to file an application for an adjustment of its base rates by June 1, 2023. North Manchester Water's last base rate increase pursuant to the alternative rate filing procedure was in Case No. 2011-00441.⁶ North Manchester Water filed an application for an adjustment of its base rates in Case No. 2019-00052, however the case was dismissed without prejudice. In the final Order in Case No. 2019-00052, the Commission stated, "The 2017 financial data is incomplete and cannot be reasonably relied upon and should not be accepted."⁷ Since that matter, North Manchester Water has only adjusted its rates pursuant to a purchased water adjustment.

To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated July 31, 2023. North Manchester Water responded to three requests for information.⁸ Additionally, Commission Staff conducted an Informal Conference on October 3, 2023,⁹ and a field review on November 8, 2023.¹⁰

⁵ Case No. 2021-00339, *Electronic Alleged Failure of North Manchester Water Association, Inc., Its Officers, Steve Davis, Carl Gregory Hoskins, Bobby Wolfe, Henry Smith, and Carl David Crawford to Comply with KRS 278.140, KRS 278.230, 807 KAR 5:006, Sec. 4, And KRS 278.990* (Ky. PSC Mar. 7, 2023), final Order. North Manchester Water was ordered to file a rate case by June 1, 2023.

⁶ Case No. 2011-00441, *Application of North Manchester Water Association for Approval of Proposed Increase in Rates for Water Service* (Ky. PSC Mar. 1, 2012), final Order.

⁷ Case No. 2019-00052, *Application of North Manchester Water Association for an Alternative Rate Adjustment* (Ky. PSC July 31, 2019), final Order.

⁸ North Manchester Water's Response to Commission Staff's First Request for Information (Staff's First Request) (filed Sept. 15, 2023); Redacted Response to Request for Information (filed Sept. 20, 2023); North Manchester Water's Response to Commission Staff's Second Request for Information (Staff's Second Request) (filed Oct. 30, 2023); North Manchester Water's Response to Commission Staff's Third Request for Information (Staff's Third Request) (filed Nov. 29, 2023).

⁹ Notice of Informal Conference (filed Sept. 25, 2023); 20231010_PSC Letter Filing IC Memo into the Record.pdf (filed Oct. 10, 2023).

¹⁰ Order (Ky. PSC Oct. 6, 2023); 20231121_PSC Letter Filing Field Review Memo into the Record.pdf (filed Nov. 21, 2023).

UNACCOUNTED-FOR WATER LOSS

The Commission notes that in its 2022 Annual Report, North Manchester Water reported a water loss of 33.3724 percent, or 70.54 million gallons.¹¹ Commission regulation 807 KAR 5:066, Section 6(3), states that for ratemaking purposes, a utility's water loss shall not exceed 15 percent of total water produced and purchased, excluding water consumed by a utility in its own operations. The table below shows that the 2022 total annual cost of water loss to North Manchester Water is \$155,593, while the annual cost of water loss in excess of 15 percent is \$85,658. The gallons of water loss in excess of 15 percent is 38.834 million. The Commission is placing greater emphasis on monitoring utilities that consistently exceed the 15 percent unaccounted-for water loss threshold. The Commission views excessive water loss as a potential warning sign of problems with the financial health and operational well-being of water utilities.¹² Commission Staff recommends a water loss surcharge, as described later in this report, to aid North Manchester Water in its water loss mitigation efforts.

Total Water Loss	Purchased Water	Purchased Power	Total
Pro Forma Purchases	\$ 422,744	\$ 43,487	\$ 466,231
Water Loss Percent	33.3724%	33.3724%	
Total Water Loss	<u>\$ 141,080</u>	<u>\$ 14,513</u>	<u>\$ 155,593</u>

Disallowed Water Loss	Purchased Water	Purchased Power	Total
Pro Forma Purchases	\$ 422,744	\$ 43,487	\$ 466,231
Water Loss in Excess of 15%	18.3724%	18.3724%	
Disallowed Water Loss	<u>\$ 77,668</u>	<u>\$ 7,990</u>	<u>\$ 85,658</u>

¹¹ 2022 Annual Report at 57.

¹² Case No. 2019-00041, *Electronic Investigation Into Excessive Water Loss by Kentucky's Jurisdictional Water Utilities* (Ky. PSC Mar. 12, 2019), Order.

DISCUSSION

Using its pro forma test-year operations, North Manchester Water determined that a base rate revenue increase of \$271,429 or 26.93 percent was necessary to achieve the revenue requirement as shown in the table below.¹³

Pro Forma Operating Expenses	\$ 1,095,825
Average Annual Principal and Interest Payments	153,161
Additional Working Capital	30,334
Overall Revenue Requirement	<u>1,279,320</u>
Less: Other Operating Revenue (Interest)	(46)
Revenue Required from Rates	<u>1,279,274</u>
Less: Pro Forma Present Rate Service Revenues	(1,007,845)
Required Revenue Increase	<u>\$ 271,429</u>
Percentage Increase	<u>26.93%</u>

To determine the reasonableness of the rates requested by North Manchester Water, Commission Staff performed a limited review of North Manchester Water's test-year operations based upon the information provided in the application and responses to requests for information. Additionally, Commission Staff conducted a field review as discussed previously. The scope of Commission Staff's review was limited to determining whether operations reported for the test year were representative of normal operations. Known and measurable¹⁴ changes to test-year operations were identified, and

¹³ North Manchester Water's Response to Deficiency Letter (filed June 22, 2023) at 68.

¹⁴ Commission regulation 807 KAR 5:076, Section 9, sets the standard for the determination of the reasonableness of proposed rates and states, in pertinent part, that the test period shall be "adjusted for known and measurable changes." See also Case No. 2001-00211, *Application of Hardin County Water District No. 1 for (1) Issuance of Certificate of Public Convenience and Necessity; (2) Authorization to Borrow Funds and to Issue its Evidence of Indebtedness Therefore; (3) Authority to Adjust Rates; and (4) Approval to Revise and Adjust Tariff* (Ky. PSC Mar. 1, 2002); Case No. 2002-00105, *Application of Northern Kentucky Water District for (A) an Adjustment of Rates; (B) a Certificate of Public Convenience and Necessity for Improvements to Water Facilities if Necessary; and (C) Issuance of Bonds* (Ky. PSC June 25, 2003); and Case No. 2017-00417, *Electronic Proposed Adjustment of the Wholesale Water Service Rates of Lebanon Water Works* (Ky. PSC July 12, 2018).

adjustments were made when their effects were deemed material. Insignificant and immaterial discrepancies were not necessarily pursued or addressed.

Commission Staff's recommendations are summarized in this report. Noah Abner and Jeff Abshire reviewed the calculation of North Manchester Water's Overall Revenue Requirement and Elizabeth Stefanski reviewed North Manchester Water's reported revenues and rate design.

SUMMARY OF FINDINGS

1. Overall Revenue Requirement and Required Revenue Increase. By applying the debt service coverage (DSC) method, as generally accepted by the Commission, Commission Staff found that North Manchester Water's required revenue from water sales is \$1,066,353 to meet the Overall Revenue Requirement of \$1,066,399 and that a \$58,507 revenue increase or 5.81 percent, to pro forma present rate revenues is necessary to generate the Overall Revenue Requirement. However, Commission Staff notes that it could not conclude that certain material items in the pro forma Schedule of Adjusted Operations (SAO) can be stated as being known and measurable. As such, Commission Staff's proposed revenue requirement does not consider potential adjustments to these items in its analysis. Commission Staff is concerned, in general, with the financial information provided by North Manchester Water, as Commission Staff was not able to reconcile reported general ledger amounts to the revenue and expense classifications that were submitted in North Manchester Water's SAO and its 2022 Annual Report filed with the Commission. North Manchester Water was also not able to provide

a reconciliation, stating such in its response to Commission Staff's third request for information.¹⁵

There are certain areas about which Commission Staff has concerns in reconciling North Manchester Water SAO. Commission Staff highlights these concerns below:

Revenues: North Manchester Water records monthly revenues in its general ledger on a cash basis and then appears to true up revenues and accounts receivable at year end to reflect accrual accounting. This practice makes it extremely difficult to determine the financial condition of the utility or track ongoing financial issues. Additionally, the utility only reports revenues as metered water sales in its general ledger. Late payment penalties and non-recurring charges are not reported separately or recorded in a separate utility account, nor could Commission Staff identify them in the revenue postings to the general ledger. The Uniform System of Accounts for Water Districts and Associations¹⁶ provides instruction on proper classification of financial transactions. Further, North Manchester Water's billing system is separate from its financial accounting system. This creates a situation where adjustments within the billing system are not visible in the revenue accounting transactions in the general ledger. Commission Staff were unable to determine whether credits and corrections reported in North Manchester Water's billing system are properly recorded in its general ledger.

General Ledger Revenue and Expense Accounts Do Not Reconcile to Schedule of Adjusted Operations Categories: Commission Staff was unable to reconcile most SAO categories to the general ledger. While Commission Staff may accept immaterial

¹⁵ North Manchester Water's Response to Staff's Third Request for Information, Item 2.

¹⁶ <https://psc.ky.gov/Home/UtilForms>.

differences, it could only identify \$60,583, or 47.6 percent of North Manchester Water's reported materials and supplies expense of \$127,280 in its review of North Manchester Water's general ledger. As noted previously, North Manchester Water could not provide a reconciliation.

Accounting Treatment of Utility Gross Receipts License Tax:¹⁷ North Manchester Water bills its customers 3 percent of billed services for a Utility Gross Receipts License Tax. Commission Staff identified \$30,918.67 in North Manchester Water's general ledger expense account No. 622, "Utility Tax". Commission Staff also reviewed the related tax filings to confirm the amounts. Additionally, Commission Staff reviewed a water invoice to a customer and confirmed that the tax billing was separate from its water rates. However, Commission Staff could neither conclude that the customer billings for the tax and the North Manchester Water's payments of the tax were recorded as revenue and expense transactions, nor as asset and liability transactions since Commission Staff was not able to reconcile the general ledger accounts to the SAO, as previously discussed.

Lease Agreement with Clay Fiscal Court: North Manchester Water has a lease agreement with the Clay County Fiscal Court (Fiscal Court) which was funded by a loan agreement between Fiscal Court and the Kentucky Infrastructure Authority (KIA). The date of the lease between the Fiscal Court and North Manchester Water is May 26, 1994.¹⁸ The date of the loan between the Fiscal Court and KIA is May 1, 1994.¹⁹ The payment transactions between North Manchester Water and the Fiscal Court and the

¹⁷ KRS 160.617, Utility Rate Increase.

¹⁸ Application, Lease Signature page at 70.

¹⁹ Application, Kentucky Infrastructure Authority Assistance Agreement at 34.

Fiscal Court and KIA are not concurrent, which, under normal circumstances, can result in slight lease/loan balance discrepancies between the parties. North Manchester Water has experienced periodic payment difficulties and made irregular and partial payments on the lease at various times. North Manchester Water stated that it had agreed to new terms with KIA.²⁰ Additionally, North Manchester Water stated that the parties had not drafted a formal agreement.²¹ However, Commission Staff notes that North Manchester Water cannot negotiate terms with a party who is not its lender, nor did it provide evidence that the underlying lease with the Fiscal Court had been modified to reflect revised terms.

Further complicating the issue, North Manchester Water stated that it had been making payments to the Fiscal Court, but that KIA had stated that it had not received them.²² Commission Staff reviewed 2021 and 2022 lease payment checks to the Fiscal Court and verified the canceled checks. If loan payments were current, based on the amortization schedule, the balance as of December 31, 2022, (the test year) would have been \$501,486.02. The stated loan balance reported by KIA (owed by the Fiscal Court) as of August 29, 2023, is \$871,483.88.²³ If loan payments were current at the time of the stated balance from KIA (assuming no significant payment delays between the Fiscal Court and KIA), the loan balance would be \$406,909.01 as of August 1, 2023.²⁴ Commission Staff is concerned that North Manchester Water does not have a clear understanding of the separate relationships in the transactions between the parties or of

²⁰ Redacted Response to Request for Information, Items 12a and 12b at 69.

²¹ North Manchester Water's Response to Staff's Second Request, Item 4 at 20.

²² Redacted Response to Request for Information, Exhibit 11 at 66.

²³ Redacted Response to Request for Information, Items 12a and 12b at 69.

²⁴ Application at 79.

the accounting for its lease payable balance to the Fiscal Court, which is independent of the accounting for the loan between the Fiscal Court and KIA.

Given the concerns highlighted above, Commission Staff recommends that North Manchester Water should work to improve its financial recordkeeping in a manner that will address the issues discussed above as well as any other issues that are noted during its independent audit process. Commission Staff recognizes that North Manchester Water has made significant improvements in its financial situation and operations since the 2019 filing. Commission Staff further recommends that North Manchester Water work to resolve payment and balance discrepancies in its lease agreement with Clay County Fiscal Court to match, subject to the payment timing differences, the outstanding loan balance between the Fiscal Court and KIA. Commission Staff also recommends that North Manchester Water be required to file a rate case with the Commission no later than October 31, 2025, based on its 2024 annual report and financial data.

2. Monthly Water Service Rates. North Manchester Water proposed a 26.93 percent increase in its revenue requirement schedule. However, its notice reflected proposed rates that would result in the average monthly amounts and percent increases shown below. The rates for an average residential customer’s monthly water bill using 4,248 gallons would increase \$10.16 from \$35.38 to \$45.74, or 28.6 percent.

Meter Size	Average Monthly Gallons	Current Rates	Proposed Rates	Increase	Percent
5/8" & 3/4" Meter	4,248	\$ 35.58	\$ 45.74	\$ 10.16	28.6%
1" Meter	14,843	\$ 101.43	\$ 142.79	\$ 41.36	40.8%
2" Meter	138,951	\$ 873.27	\$ 1,279.62	\$ 406.36	46.5%
3" Meter	180,870	\$ 1,133.83	\$ 1,663.60	\$ 529.77	46.7%

North Manchester Water did not perform a cost-of-service study (COSS). North Manchester Water stated that it did not complete a COSS at this time, but determined that a study was not necessary as the system had no material changes.²⁵ The Commission has previously found that the allocation of a revenue adjustment evenly across a utility's rate design is appropriate when there has been no evidence entered into the record demonstrating that this method is unreasonable and in the absence of a COSS. Finding no such evidence in this case, Commission Staff followed the method proposed by North Manchester Water and allocated the \$58,507 revenue increase across North Manchester Water's rate design. Commission Staff calculated rates for each meter classification as shown below. The rates for an average residential customer's monthly water bill using 4,248 gallons would increase \$2.07 from \$35.58 to \$37.65, or 5.8 percent. Including the proposed water loss reduction surcharge of \$3.63 per month, the average bill would increase \$5.70 from \$35.58 to \$41.28, or 16.02 percent.

Meter Size	Average Monthly Gallons	Current Rates	Commission Staff Calculated Rates	Increase	Percent
5/8" & 3/4" Meter	4,248	\$ 35.58	\$ 37.65	\$ 2.07	5.8%
1" Meter	14,843	\$ 101.43	\$ 107.32	\$ 5.88	5.8%
2" Meter	138,951	\$ 873.27	\$ 923.84	\$ 50.57	5.8%
3" Meter	180,870	\$ 1,133.83	\$ 1,199.50	\$ 65.67	5.8%

²⁵ North Manchester Water's Response to Staff's First Request, Responses_to_PSC_DR1_Redacted.pdf, Item 22.

3. Nonrecurring Charges. Following the Commission's recent decisions,²⁶ Commission Staff has reviewed North Manchester Water's Nonrecurring Charges. The Commission found that because personnel are currently paid during normal business hours, estimated labor costs previously included in determining the amount of Nonrecurring Charges should be eliminated from the charges. North Manchester Water provided the cost justification information for the nonrecurring charges,²⁷ Commission Staff reviewed the cost justification information provided by North Manchester Water and adjusted these charges by removing the \$18.45 per hour Field Labor Costs and the \$16.62 per hour Office/Clerical Labor Costs from those charges that occur during normal business hours. The calculation of these adjustments to Nonrecurring Charges are included in a table provided in Appendix A. North Manchester Water also provided information about the Returned Check Charge,²⁸ to which Commission Staff adjusted the charge to zero, as North Manchester Water's bank no longer charges it a fee for a returned check. These adjustments result in the following revised Nonrecurring Charges:

²⁶ Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020); Case No. 2020-00167, *Electronic Application of Ohio County Water for an Alternative Rate Adjustment* (Ky. PSC Dec. 3, 2020); Case No. 2020-00196, *Electronic Application of West Daviess County Water for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020); and Case No. 2020-00195, *Electronic Application of Southeast Daviess County Water for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020).

²⁷ North Manchester Water's Response to Staff's First Request, Item 19, and North Manchester Water's Response to Staff's Second Request, Item 20.

²⁸ North Manchester Water's Response to Staff's Second Request, Item 20.

Description	Current Tariff	Revised Rate
Late Payment Penalty	10%	10%
Disconnection Charge	\$45.00	\$15.00
Reconnection Charge	\$45.00	\$15.00
Returned Check Charge	\$20.00	\$0.00
Service Call / Investigation	\$45.00	\$15.00
Service Call / Investigation After Hours	\$55.00	\$74.00
Meter Test Request	\$75.00	\$15.00

No adjustments were made in Other Operating Revenue for the changes to nonrecurring charges, due to the revenue accounting issues discussed previously.

4. Water Loss Reduction Surcharge. North Manchester Water did not propose a Water Loss Surcharge in its application. Based on North Manchester Water's water loss history for 2018 through 2022,²⁹ Commission Staff recommends a Water Loss Surcharge be implemented to aid North Manchester Water in its water loss mitigation efforts. The use of a surcharge is consistent with prior Commission action in cases involving water utilities with excessive unaccounted-for water loss.³⁰ Recognizing prior Commission precedent to allow the use of surcharges to assist utilities in obtaining the proper funding needed to address water loss, Commission Staff calculated a Water Loss Surcharge using information from North Manchester Water's 2022 Annual Report.

²⁹ 2018 Annual Report, 2019 Annual Report, 2020 Annual Report, 2021 Annual Report, and 2022 Annual Report.

³⁰ See Case No. 96-126, *An Investigation into the Operations and Management of Mountain Water District* (Ky. PSC Aug. 11, 1997); Case No. 2011-00217, *Application of Cannonsburg Water District for (1) Approval of Emergency Rate Relief and (2) Approval of the Increase in Nonrecurring Charges* (Ky. PSC June 4, 2012); Case No. 2018-00017, *Application of Martin County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 5, 2018); Case No. 2018-00429, *Application of Graves County Water District for an Alternative Rate Adjustment* (Ky. PSC Sept. 30, 2019); and Case No. 2019-00119, *Electronic Application of Estill County Water District No. 1 for a Surcharge to Finance Water Loss Control Efforts* (Ky. PSC Mar. 24, 2010); Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020), Order at 11-13.

Commission Staff recommends a water loss reduction surcharge of \$3.63 per month per customer for 48 months or upon billing of \$342,904 for the life of the surcharge. Due to the revenue accounting issues previously discussed, Commission Staff recognizes potential concerns in recommending implementation, even with the restrictions and monitoring that the Commission typically places on surcharge cases. However, the overall fiscal health and stability of a water utility is paramount to the continued health and safety of customers.

Description	Amount
Disallowed Water Loss	\$ 85,658
Months	12
Customers	1,968
Surcharge Per Customer Per Month	\$ 3.63
Surcharge Months	48
Customers	1,968
Grand Total Surcharge	<u>\$ 342,904</u>

In keeping with Commission practice, Commission Staff recommends that the Commission establish a separate proceeding to monitor the surcharge, place strict controls over the use of the funds that will be collected from the surcharge, and require North Manchester Water to develop a long-term plan to combat water loss within four months of the final Order in this proceeding.

PRO FORMA OPERATING STATEMENT

North Manchester Water’s Pro Forma Operating Statement for the test year ended December 31, 2022, as determined by Commission Staff appears in the table below. Commission Staff noted each expense category for which it could not determine a pro forma amount. As noted above, Commission Staff did not propose any adjustments to revenues because it was unable to resolve numerous reconciliation issues between the

general ledger and other information sources. Further, pro forma adjustments for a historical test period should represent known and measurable changes.

	Test Year	North Manchester Water Proposed Adjustments	Commission Staff Adjustments	Total Adjustments (Ref.)	Pro Forma
Operating Revenues					
Sales of Water	\$ 1,007,846			0	\$ 1,007,846
Other Water Revenues	46			0	46
Total Operating Revenues	1,007,892	0	0	0	1,007,892
Operating Expenses					
Operation and Maintenance Expenses					
Salaries and Wages - Employees	201,412	6,042	(40,771)	(34,729) (A)	166,683
Employee Pensions and Benefits	30,655	920	(5,076)	(4,156) (B)	
			(5,830)	(5,830) (B)	20,669
Purchased Water	427,607	12,828	(17,691)	(4,863) (C)	
			(77,668)	(77,668) (C)	345,076
Purchased Power for Pumping	43,851	1,316	(1,680)	(364) (D)	
			(7,990)	(7,990) (D)	35,497
Materials and Supplies	127,280	1,406	(1,406)	0 (E)	127,280
Contractual Services	38,231	1,537	(1,537)	0 (F)	38,231
Transportation Expense	27,426	87		87 (G)	27,513
Insurance	22,167	665	2,307	2,972 (H)	25,139
Miscellaneous Expense	15,742	1,618	(1,618)	0 (I)	15,742
Total Operation and Maintenance Expenses:	934,371	26,419	(158,960)	(132,541)	801,830
Taxes Other Than Income - FICA	23,781			0 (J)	23,781
Depreciation	111,254	0	(10,203)	(10,203) (K)	
			(18,364)	(18,364) (K)	82,687
Total Operating Expenses	1,069,406	26,419	(187,527)	(161,108)	908,298
Income Available to Service Debt	\$ (61,514)	\$ (26,419)	\$ 187,527	\$ 161,108	\$ 99,594

(A) Salaries and Wages - Employees. North Manchester Water proposed an increase of \$6,042, or 3.0 percent, but did not provide a reason for the adjustment or evidence of a known and measurable change to the test period expenses. North Manchester Water was granted confidential treatment of employee wage information in an Order dated September 9, 2023.³¹ Therefore, calculation details provided in this report are limited. Commission Staff reviewed the information provided by North Manchester Water and calculated a decrease of \$34,729 from test-year salaries as shown below.

³¹ Order (Ky. PSC Sept. 9, 2023).

Commission Staff calculations are based on the projected staffing level, projected hours, which reflects a decrease from the test year, and current wage rates. Commission Staff recommends the Commission accept the Commission Staff's proposed adjustment because it reflects information provided in North Manchester Water's application and responses to information requests.

Description	Amount
Test Year	\$ 201,412
Adjustment	(34,729)
Pro Forma	<u>\$ 166,683</u>

(B) Employee Pensions and Benefits. North Manchester Water pays 100 percent of single medical insurance coverage for full time employees. North Manchester Water proposed an increase of \$920, or 3.0 percent, but did not provide a known and measurable reason for the adjustment. Commission Staff reviewed the information provided by North Manchester Water and calculated a cost decrease of \$4,156 based on current cost information provided by North Manchester Water. Additionally, keeping with Commission precedent, Commission Staff calculated a reduction of \$5,830 to reflect allowable health insurance premium based on the Bureau of Labor Statistics (BLS).³² A summary of the amounts is shown below. Commission Staff recommends the Commission accept the proposed adjustment because it reflects information provided in North Manchester Water's application and responses to data requests.

³² See Case No. 2017-00263, *Electronic Application of Kentucky Frontier Gas, LLC for Alternative Rate Adjustment* (Ky. PSC Dec. 2, 2017), at 9-10.

Description	Amount
Monthly Single Premium Coverage	\$ 2,208.29
	12
Annual (rounded to zero)	\$ 26,499
Test Year	(30,655)
Increase / (Decrease)	<u>\$ (4,156)</u>
BLS Employee Contribution Rate	<u>22%</u>
Employee Contribution Dollars	<u>\$ (5,830)</u>

(C) Purchased Water. North Manchester Water proposed an increase of \$12,828, or 3.0 percent, but did not provide a known and measurable reason for the adjustment. Commission Staff calculated the test year gallons purchased which resulted in a decrease of \$4,863 as shown below.

Description	Amount
Gallons	211,371,900
Current Purchase Rate	\$ 2.00
Pro Forma Cost	\$ 422,744
Test Year Purchase Cost ()	(427,607)
Increase in Purchase Cost	<u>\$ (4,863)</u>

Additionally, Commission Staff reduced purchased water expense by \$77,668 for ratemaking purposes for water loss in excess of 15 percent as shown below.

Disallowed Water Loss	Purchased Water	Purchased Power	Total
Pro Forma Purchases	\$ 422,744	\$ 43,487	\$ 466,231
Water Loss in Excess of 15%	18.3724%	18.3724%	
Disallowed Water Loss	<u>\$ 77,668</u>	<u>\$ 7,990</u>	<u>\$ 85,658</u>

Commission Staff recommends the Commission approve the Commission Staff's proposed adjustment to decrease cost by \$4,863 and the Commission Staff's proposed adjustment to disallow excess water loss cost of \$77,668 for ratemaking purposes.

(D) Purchased Power for Pumping. North Manchester Water proposed an increase of \$1,316, or 3.0 percent, but did not provide a known and measurable reason for the adjustment. Commission Staff reviewed the posting to the general ledger and determined that charges were recorded to Delta Natural Gas Company and Woods Sanitation that are not related to power for pumping resulting in a net cost reduction of \$364 as shown below.

Description	Amount	Pro Forma
Delta	\$ 2,359.98	
Jackson Energy	8,670.64	(1)
Kentucky Utilities	34,816.83	(1)
Woods San	202.00	
General Ledger Components	<u>46,049.45</u>	
(1) Pro Forma Power for Pumping	\$ 43,487.00	
Reported Test Year Power for Pumping	(43,851.00)	
Adjustment to Test Year	<u>\$ (364.00)</u>	

Additionally, Commission Staff reduced purchased power expense by \$7,990 for ratemaking purposes for water loss in excess of 15 percent as shown in the previous table that describes Purchased Water adjustments for excess water loss. Commission Staff recommends the Commission approve both Commission Staff's proposed adjustments.

(E) Materials and Supplies. North Manchester Water proposed an increase of \$1,406, or 1.1 percent, but did not provide a known and measurable reason for the adjustment. As described earlier in this report, the test year amount for materials and supplies could not be reconciled to the general ledger based on the method of accounting of expenses, however, the Commission Staff did not propose an adjustment based on the

concerns with the general ledger. Commission Staff recommends that the Commission not accept the proposed adjustment because it is not known and measurable.

(F) Contractual Services. North Manchester Water proposed an increase of \$1,537, or 4.0 percent, but did not provide support for the adjustment. Commission Staff recommends that the Commission not accept the proposed adjustment because it is not known and measurable.

(G) Transportation Expense. North Manchester Water proposed an increase of \$87, or 0.3 percent, but did not provide support for the adjustment. Commission Staff recommends that the Commission accept the proposed adjustment because it is not material.

(H) Insurance. North Manchester Water proposed an increase of \$665, or 3 percent, but did not provide support for the adjustment. Commission Staff reviewed insurance invoices provided by North Manchester Water in its responses to Staff's Third Request³³ and calculated an increase of \$2,972 as shown below. Commission Staff recommends that the Commission accept the Commission Staff's proposed adjustment because it is based on information submitted into the record that is known and measurable.

³³ Response to Commission Staff's Third Request, Item10.

Description	Amount
Liability	6,753.78
Property	3,233.04
Workers' Comp	2,582.59
Semi-Annual	12,569.41
x two	2
Annual	\$ 25,139
Test Year ()	\$ (22,167)
Increase / (Decrease)	<u>\$ 2,972</u>

(I) Miscellaneous Expense. North Manchester Water proposed an increase of \$1,618, or 10.3 percent, of the test year amount of \$15,742, but did not provide support for the adjustment. Commission Staff recommends that the Commission not accept the proposed adjustment because it is not known and measurable.

(J) Taxes Other Than Income. North Manchester Water did not propose any adjustments. The test year amount of \$23,781 could not be reconciled to the general ledger and North Manchester Water. Commission Staff calculated FICA taxes of \$12,751 but cannot reasonably conclude that it has captured the entirety of taxes that should be reported in the pro forma. Commission Staff recommends that the Commission accept the unadjusted test year amount of \$23,781.

(K) Depreciation Expense. North Manchester Water provided a summary of depreciation with its application which reflected depreciation expense of \$101,051 and a depreciation decrease adjustment of \$18,364.³⁴ However, it did not recommend any adjustments to depreciation expense. In its response to a deficiency letter, it provided its Federal Form 4562, Depreciation and Amortization Report, which contains a detailed asset listing, and was filed with its 2022 Federal Income Tax Return. Form 4562 reflected

³⁴ Application, unnumbered page 21 of 114.

depreciation expense of \$111,254 which is also the amount that North Manchester Water reported for its test year in its Schedule of Adjusted Operations, which was submitted with the same response to deficiency.³⁵ Commission Staff reduced test year depreciation by \$10,203 to \$101,051, which is the book amount provided in North Manchester Water’s application. Commission Staff also made an adjustment of asset service lives to the midpoint of service life ranges set forth in the National Association of Regulatory Utility Commissioners’ (NARUC) publication titled “Depreciation Practices for Small Water Utilities” (NARUC Study). Commission Staff’s adjustment for the presumed NARUC decrease is \$18,364 as shown in the table below. Commission Staff recommends the Commission approve the proposed reduction of \$10,203 to correct test-year depreciation expense and the proposed reduction of \$18,364 to adjust depreciation to reflect the midpoint life ranges set forth in the NARUC Study.

Description	Amount
Corrected Test Year Depreciation	\$ 101,051
Test Year Amount ()	(111,254)
Commission Staff Adjustment	<u>\$ (10,203)</u>
NARUC Adjustment	<u>\$ (18,364)</u>

OVERALL REVENUE REQUIREMENT

The Commission has historically applied a Debt Service Coverage (DSC) method to calculate the Overall Revenue Requirement of water districts and water associations. This method allows for recovery of (1) cash-related pro forma operating expenses; (2)

³⁵ Response to Deficiency Letter (filed June 22, 2023), at 9.

recovery of depreciation expense, a non-cash item, to provide working capital;³⁶ (3) the average annual principal and interest payments on all long-term debts; and (4) working capital that is in addition to depreciation expense.

	Manchester Water Association Commission Staff	
Pro Forma Operating Expenses	\$ 1,095,825	\$ 908,298
Average Annual Principal and Interest Payments	153,161	131,751 (1)
Additional Working Capital	30,334	26,350 (2)
Overall Revenue Requirement	1,279,320	1,066,399
Less: Other Operating Revenue (Interest)	(46)	(46)
Revenue Required from Rates	1,279,274	1,066,353
Less: Pro Forma Present Rate Service Revenues	(1,007,845)	(1,007,846)
Required Revenue Increase	<u>\$ 271,429</u>	<u>\$ 58,507</u>
Percentage Increase	<u>26.93%</u>	<u>5.81%</u>

1. Average Annual Principal and Interest Payments. At the time of Commission Staff's review, North Manchester Water had one lease agreement with the Clay County Fiscal Court and one finance agreement for the purchase of a vehicle. North Manchester Water proposed a five-year average debt service from 2022 through 2026 of \$151,662. However, it assumed a full year of lease payments to the Fiscal Court during 2026 and excluded payments on the vehicle loan. The amount submitted in its revenue

³⁶ The Kentucky Supreme Court has held that the Commission must permit a water district to recover its depreciation expense through its rates for service to provide internal funds for renewing and replacing assets. See *Public Serv. Comm'n of Kentucky v. Dewitt Water Dist.*, 720 S.W.2d 725, 728 (Ky. 1986). Although a water district's lenders require that a small portion of the depreciation funds be deposited annually into a debt reserve/depreciation fund until the account's balance accumulates to a required threshold, neither the Commission nor the Court requires that revenues collected for depreciation be accounted for separately from the water district's general funds or that depreciation funds be used only for asset renewal and replacement. The Commission has recognized that the working capital provided through recovery of depreciation expense may be used for purposes other than renewal and replacement of assets. See Case No. 2012-00309, *Application of Southern Water and Sewer District for an Adjustment in Rates Pursuant to the Alternative Rate Filing Procedure for Small Utilities* (Ky. PSC Dec. 21, 2012).

requirement was reported at \$153,161. Commission Staff recommends a three-year average which results in average debt service of \$131,751 for the period from 2024 through 2026 as shown below. A three-year average better aligns the debt service portion of the revenue requirement with the frequency that North Manchester Water should adjust its rates. The difference in lease payments to the Fiscal Court in 2026 is because Commission Staff based its calculations on the amortization schedule for the lease which, based on its original terms, is scheduled to be retired on June 1, 2026. Commission Staff does not have a known and measurable basis to support a longer payment term in the absence of documented modifications to its lease agreement with the Fiscal Court, including an updated amortization schedule, to reflect the correct loan balance and revised KIA loan maturity date.

Description	2022	2023	2024	2025	2026	Average
Application Table B	\$ 152,131	\$ 151,920	\$ 151,579	\$ 151,291	\$ 151,391	\$ 151,662
Commission Staff Calculation						
Lease with Fiscal Court			151,579	151,291	75,535	
Vehicle Purchase			5,616	5,616	5,616	
Total / Three-Year Average			\$ 157,195	\$ 156,907	\$ 81,151	\$ 131,751
North Manchester Water Revenue Requirements Amount						(153,161)
Difference						\$ (21,410)

Additional Working Capital. The DSC method, as historically applied by the Commission, includes an allowance for additional working capital that is equal to the minimum net revenues required by a district’s lenders that are above its annual average debt payments. North Manchester Water requested recovery of an allowance for working capital that is equal to 120 percent of its average annual payments, or \$30,334. Commission Staff recalculated the working capital requirement based on the pro forma

debt service adjustment described above resulting in a working capital amount of \$26,350.

Signatures:

/s/ Noah Abner

Prepared by: Noah Abner
Revenue Requirements Branch
Division of Financial Analysis

/s/ Jeff Abshire

Prepared by: Jeff Abshire
Revenue Requirements Branch
Division of Financial Analysis

/s/ Elizabeth Stefanski

Prepared by: Elizabeth Stefanski
Rate Design Branch
Division of Financial Analysis

APPENDIX A

APPENDIX TO COMMISSION STAFF'S REPORT OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2023-00183 DATED JAN 11 2024

* Denotes Rounding

Nonrecurring Charges Adjustments

	<u>Disconnection Charge</u>	
	<u>Utility Revised Charge</u>	<u>Staff Revised Charge</u>
Field Materials		
Field Labor (\$18.45 @ 1 hr x 2 employee)	\$36.90	
Office Supplies		
Office Labor	\$8.31	
Transportation (22 miles @ 0.655)	\$14.00	\$14.00
Misc.		
Total Revised Charge	<u>\$59.21</u>	<u>\$14.00</u>
Current Rate	\$45.00	

	<u>Reconnection Charge</u>	
	<u>Utility Revised Charge</u>	<u>Staff Revised Charge</u>
Field Materials		
Field Labor (\$18.45 @ 1 hr x 2 employee)	\$36.90	
Office Supplies		
Office Labor	\$8.31	
Transportation (22 miles @ 0.655)	\$14.00	\$15.00
Misc.		
Total Revised Charge	<u>\$59.21</u>	<u>\$15.00</u>
Current Rate	\$45.00	

	<u>Returned Check Charge</u>	
	<u>Utility Revised Charge</u>	<u>Staff Revised Charge</u>
Field Materials		
Field Labor (\$20.00 at 1 hour)		
Office Supplies		
Office Labor (\$16.62 at 2 hours)	\$33.24	\$0.00
Transportation		
Misc.		
Total Revised Charge	<u>\$34.00</u>	<u>\$0.00</u>
Current Rate	\$20.00	

<u>Service Call/Investigation</u>		
	<u>Utility Revised Charge</u>	<u>Staff Revised Charge</u>
Field Materials		
Field Labor (\$21.28 at 2 hours)	\$42.56	
Office Supplies		
Office Labor (\$16.62 at 1 hour)	\$16.62	
Transportation (22 miles @ 0.655)	\$14.00	\$15.00
Misc.		
Total Revised Charge	<u>\$73.00</u>	<u>\$15.00</u>
Current Rate	\$45.00	

<u>Service Call/Investigation (after hours)</u>		
	<u>Utility Revised Charge</u>	<u>Staff Revised Charge</u>
Field Materials		
Field Labor (\$29.91 at 2 hours)	\$59.82	\$60.00
Office Supplies		
Office Labor (\$16.62 at 1 hour)	\$16.62	\$0.00
Transportation (22 miles @ 0.655)	\$14.00	\$15.00
Bank Charge		
Total Revised Charge	<u>\$90.00</u>	<u>\$75.00</u>
Current Rate	\$55.00	

<u>Meter Test Charge</u>		
	<u>Utility Revised Charge</u>	<u>Staff Revised Charge</u>
Field Materials		
Field Labor (\$21.28 at 3 hours)	\$63.84	
Office Supplies		
Office Labor (\$16.62 at 1 hour)	\$16.62	
Transportation (22 miles @ 0.655)	\$14.00	\$15.00
Misc.		
Total Revised Charge	<u>\$95.00</u>	<u>\$15.00</u>
Current Rate	\$75.00	

APPENDIX B

APPENDIX TO COMMISSION STAFF'S REPORT OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2023-00183 DATED JAN 11 2024

Monthly Water Rates

5/8-inch & 3/4-inch Meter

First	2,000 Gallons	\$22.86	Minimum Bill
Over	2,000 Gallons	\$0.00658	Per Gallon

1-inch Meter

First	5,000 Gallons	\$42.55	Minimum Bill
Over	5,000 Gallons	\$0.00658	Per Gallon

2-inch Meter

First	15,000 Gallons	\$108.24	Minimum Bill
Over	15,000 Gallons	\$0.00658	Per Gallon

3-inch Meter

First	30,000 Gallons	\$206.78	Minimum Bill
Over	30,000 Gallons	\$0.00658	Per Gallon

Nonrecurring Charges

5/8 x 3/4 Inch Water Tap On All Larger Meters	\$1,414.00 Actual Cost
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Late Payment Penalty	10%
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Disconnection Charge	\$15.00
Reconnection Charge	\$15.00
Returned Check Charge	\$0.00
Service Call / Investigation	\$15.00
Service Call / Investigation After Hours	\$74.00
Meter Test Request	\$15.00
Damage to Meter Setting or Lid	Actual
Meter Relocate	Actual

Water Loss Reduction Surcharge; limited to 48 months	\$3.63 Per Month
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