COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ALTERNATIVE RATE ADJUSTMENT FILING OF MARION COUNTY WATER DISTRICT	))	CASE NO. 2016-00163

ORDER

By this Order, the Commission approves an increase to Marion County Water District's ("Marion District") water service rates. The approved water rates will generate $78,913 in additional annual revenues, a 3.15 percent increase to pro forma present rate water sales revenues in the amount of $2,503,565. The monthly water bill of a typical residential customer[1] will increase from $29.11 to $30.50, an increase of $0.94, or 3.2 percent.

On May 12, 2016, the Commission accepted for filing Marion District's Application ("Application") for a rate adjustment pursuant to 807 KAR 5:076. In the Application, Marion District requested to increase its monthly water service rates in order to generate $307,911 in additional annual revenues, a 12.3 percent increase. No person requested leave to intervene in this proceeding.

Commission Staff ("Staff") applied methods and practices that are generally accepted by the Commission to review the reasonableness of Marion District's current and proposed water service rates. On August 11, 2016, Staff issued a report summarizing its findings. Staff found that Marion District's adjusted test-year operations

[1] A typical residential customer purchases 4,000 gallons of water per month through a 5/8- x 3/4-inch meter.

support a 3.15 percent increase to annual water sales revenues. The water service rates calculated by Staff were presented in its report at Attachment A.

On August 22, 2016, Marion District filed with the Commission its written comments to Staff's report wherein Marion District disputed Staff's proposed accounting and ratemaking treatment of pension costs reported pursuant to Governmental Accounting Standards Board ("GASB") Statement No. 68 ("GASB 68") and Staff's proposal to change the depreciable life assigned to transmission and distribution mains from 40 and 50 years to 62.5 years. An informal conference ("IC") was held on September 1, 2016, to discuss Marion District's comments. A memorandum was filed into the record on September 9, 2016, ("IC memo") summarizing the discussions at the IC. Marion District filed comment to the IC memo on September 16, 2016. Marion District did not request that a formal hearing be held and this case was submitted for a decision on the evidence of record.

Marion District provides pension benefits and post-retirement health care benefits to its employees by participating in the County Employee Retirement System ("CERS"), a cost-sharing plan wherein the post-retirement obligations of the employees of more than one employer are pooled and the plan's assets can be used to pay the benefits of the employees of any participating member. As a participating member, Marion District is required to contribute a percentage of its employee wages to CERS.[2] Marion District's test-year contributions to CERS totaled $48,953.[3]

Prior to the test year, Marion District reported the cost of employee pensions and post-retirement health care benefits pursuant to GASB Statement No. 27 ("GASB 27"). GASB 27 required that Marion District report its contributions to CERS as employee retirement expense. GASB 27 did not require that Marion District report a liability on its financial statements for a portion of either CERS's Net Pension Liability ("NPL") or CERS's unfunded post-retirement health care liability.[4]

The accounting and reporting requirements for the CERS pension benefit changed during the test year due to the passage and implementation of GASB 68. The accounting for post-retirement health care costs did not change. GASB 68 required that Marion District report the following for pensions during the test year:

1) A charge against Retained Earnings to account for the cumulative effect of the change from GASB 27 to GASB 68;

2) Marion District's proportionate share of the CERS NPL;

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[2] The table below summarizes the CERS contribution rates for each of the last five fiscal years ending June 30.

Fiscal Year Ending June 30,	Employer Contribution Rate
2012	18.96%
2013	19.55
2014	18.89
2015	17.67
2016	17.06

[3] Staff Report at 7.

[4] *Id.* at 10.

3) Deferred Inflow of Resources and Deferred Outflow of Resources related to Pensions; and

4) Annual pension expense that includes:

a. pension contributions to CERS during the reporting period that occur prior to June 30, 2015, the NPL's measurement date;

b. the amortization of Marion District's proportionate share of Deferred Outflows and Deferred Inflows related to pensions;

c. Marion District's proportionate share of the plan's actuarially determined annual pension expense; and

d. the increase or decrease that occurred during the reporting period to the amount of Marion District's proportionate share of the CERS NPL.[5]

To implement GASB 68 during the test year, Marion District relied on the results of the CERS actuarial valuation for the fiscal year ended June 30, 2014, because the actuarial valuation for June 30, 2015, had not been completed and published at the time Marion District closed its books of original entry in preparation for the audit of its test-year financial statements. Using the 2014 actuarial valuation, Marion District reported the following to implement GASB 68.[6]

NPL	$ 376,000
Retained Earnings	(366,435)
Deferred Outflows	67,904
Deferred Inflows	42,000
Retirement Expense	32,614

[5] *Id.* at 11–13.

[6] *Id.* at 19–20. Note that the CERS Retirement Expense in the amount of $32,614 includes pension costs and post-retirement health care cost.

In the Application, Marion District requested to increase its test-year CERS employee retirement expense by $126,250,[7] from $32,614 to $158,864. It calculated the adjustment using the portion of the CERS 2015 actuarial valuation that was available to it at the time it filed the Application with the Commission.[8]

In its report, Staff found that Marion District's test-year implementation of GASB 68 using the June 30, 2014 actuarial valuation was in violation of GASB 68, Paragraph 48, which required that Marion District use the June 30, 2015 actuarial valuation. Using the correct actuarial valuation, Staff determined that Marion District should have reported the following to implement GASB 68 during the test year.[9]

NPL			$	510,592
Retained Earnings				(358,052)
Deferred Outflows				66,576
Deferred Inflows				-
Retirement Expense for:				
Pensions	$	121,210		
Health Care Costs		13,707		134,917

Staff further found that Marion District should not recover through rates the $134,917 test-year retirement expense calculated by Staff, or the amount proposed by Marion District. Instead, Staff found that Marion District should recover the amount of its test-year CERS contributions, $48,953, and report the $85,964 difference between these contributions and the retirement expense calculated by Staff as a Regulatory Asset as allowed by GASB 62.

[7] Application, ARF Form 1 – Attachment SAO-W, Ref. A.

[8] Staff Report at 24.

[9] *Id*. at 20–23.

Staff explained that, pursuant to its method, the test-year expense calculated using the 2015 actuarial valuation is reduced from $134,917 to $48,953 for accounting purposes and for ratemaking purposes. The Regulatory Asset account is used to report: 1) the difference between the amount of the GASB 68 pension expense and the amount of test-year contributions; 2) the cumulative effect on Retained Earnings of the change from GASB 27 to GASB 68; and 3) the Deferred Inflows and Deferred Outflows related to pensions. The Regulatory Asset account will be adjusted annually in each reporting period after the test year. The Regulatory Asset account's balance at the end of each reporting period would mirror the balance of the NPL reported by Marion District for that period. When the NPL becomes fully funded, the balance of the Regulatory Asset will be zero and Marion District will have recovered through rates its contributions to CERS to fund Marion District's NPL.[10] Staff's method results in Marion District reporting retirement costs for the test-year end as follows:

Regulatory Asset	$	510,592
NPL		510,592
Retained Earnings		-
Deferred Outflows		-
Deferred Inflows		-
Retirement Expense		48,953

Staff explained that its proposed accounting and ratemaking treatment of GASB 68 would mitigate the impact of GASB 68 on Marion District's Balance Sheet by restoring Retained Earnings to its original balance prior to implementation of GASB 68 and by providing a Regulatory Asset to offset the NPL. Staff further explained that its method would smooth the level of annual pension expense reported by Marion District

[10] *Id.* at 24–27.

in future reporting periods since the annual expense will always be equal to the contributions to CERS, which have been historically constant.[11] To account for the effects of Staff's proposed treatment of GASB 68, Staff increased test-year retirement expense by $16,339, from $32,614 to $48,953, the amount of Marion District's test-year contributions to CERS.[12]

Marion District disagreed with Staff's findings. It stated that the "pension liability as reflected on the audit report has been properly computed and reported"[13] and that Staff's proposal "does not address the reporting requirements that we are governed by."[14] Marion District stated that Staff's proposal "has the impact of ignoring GASB 68 completely."[15] Marion District questioned how it will fund the pension liability if it is not built into rates.[16]

During the test year, Marion District depreciated water transmission and distribution mains that were installed during the years 1970 through 2007 using a 50-year depreciable life. It depreciated mains installed from 2008 through 2015 using a 40-year life. Staff adjusted the depreciable life assigned to all mains to 62.5 years, the midpoint of the 50- to 75-year life range for mains found appropriate by the National Association of Regulatory Utility Commissioners ("NARUC") in its 1979 publication titled

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[11] *Id.* at 26.

[12] *Id.* at 7.

[13] Marion District's August 22, 2016 Response to Staff's Report at 2.

[14] *Id.* at 2–3.

[15] *Id.* at 3.

[16] Marion District's September 16, 2016 Comments to the IC Memo at 1.

Deprecation Practices for Small Water Utilities ("NARUC Study").[17] To account for the change to the depreciable lives assigned to mains, Staff reduced test-year depreciation expense by $66,828.[18]

In its report, Staff explained that the Commission requires a "large" utility to perform a depreciation study to determine the appropriate depreciable lives to be assigned to each of its utility plant account groups. Detailed property records specific to historic plant additions, plant retirements, and salvage practices are required to complete a depreciation study. Generally, "small" water utilities, such as Marion District, do not maintain property records with enough detail to properly complete a formal study. Even when adequate records are maintained, "small" utilities do not have the financial resources to fund a formal study. Therefore, to evaluate the reasonableness of the

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[17] Staff Report at 31.

[18] *Id.* at 28. The adjustment shown in Staff's Report totals $66,828. Staff's adjustment includes the impact of changing the depreciable lives assigned to mains in service as of the end of the test year, and it includes depreciation that will accrue on mains placed into service subsequent to the test year, but before the issuance of Staff's report. The total adjustment is detailed below.

	Main In Service		
	Test Year	Subsequent to Test Year	Total
Cost	$12,245,513	$ 42,902	$12,288,415
Divide by: Depreciable Life	62.5	62.5	62.5
Pro Forma Depreciation	195,928	686	196,615
Less: Test Year	(262,756)	-	(262,756)
Adjustment	$ (66,828)	$ 686	$ (66,141)

depreciation practices of small water utilities, the Commission has historically relied on the NARUC Study.[19]

Staff further explained that, when evaluating a water district's depreciable lives, the Commission considers an asset group's construction materials, condition, and other factors to determine the appropriate depreciable life for each asset account group that falls inside or outside the NARUC ranges. The Commission has assigned lives at the short end and long end of the NARUC ranges when evidence is presented to support such lives and, when warranted, the Commission has used lives that fall outside the NARUC ranges. When no evidence exists to support a specific life that is inside or outside the NARUC ranges, the Commission has used the mid-point of the ranges to depreciate utility plant.[20]

In this proceeding, Staff found no evidence to support depreciable lives that vary significantly from the mid-point of the NARUC ranges except for the life assigned to Marion District's automated metering system.[21] Staff found that the 20-year depreciable life Marion District assigned to its metering system was appropriate. Staff further found that the lives assigned to all other asset account groups, except for mains, were close enough to the mid-point that adjustments to the mid-point would not have a material effect on Marion District's test-year depreciation expense. Accordingly, Staff adjusted only the life assigned to mains.[22]

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[19] *Id.* at 28–29.

[20] *Id.* at 28–31.

[21] The depreciable life range stated in the NARUC Study for meters is 35–45 years.

[22] Staff Report at 31–32.

Marion District disagreed with Staff's depreciation of mains. Marion District questioned the reasonableness of Staff's application of the NARUC Study in this proceeding. Marion District stated that it is much larger than the water utilities for which the NARUC Study was designed, noting that the study was created to assist in the development of the depreciation practices of small utilities that have less than: 1) 200 customers; 2) $50,000 in annual revenue; and 3) $1,000,000 in plant investment.[23] Marion District noted that the NARUC Study was performed in 1979 and could not have adequately taken into account the effects of mains constructed of polyvinyl chloride ("PVC"), which Marion District asserted became prevalent in the mid-1970s and represents a significant portion of the main in its distribution system.[24]

Marion District further argued that the Commission had previously approved the 50-year depreciable life for its mains in Case No. 7901[25] and that this life should not be changed in this proceeding.[26] Marion District supported the continued use of the 50-year life by comparing its operations to those of Southern Water and Sewer District ("Southern District"), which the Commission, in Case No. 2012-00309,[27] allowed a 50-year depreciable life for mains in recognition that Southern District's mains had decayed at an accelerated rate. Marion District stated that its operating characteristics are

[23] Marion District's August 22, 2016 Response to Staff's Report at 1.

[24] IC Memo at 2.

[25] Case No. 7901, *General Adjustment of Rates of Marion County Water District, Effective July 21, 1980* (Ky. PSC Nov. 21, 1980).

[26] Marion District's August 22, 2016 Response to Staff's Report at 2; IC Memo at 3, and Marion District's September 16, 2016 Comments to the IC Memo at 2.

[27] 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 July 12, 2013).

similar to those of Southern District and that there is evidence that its mains have also deteriorated at an accelerated rate. In support of its position, Marion District stated that some of the PVC main it installed during the 1970s have become extremely brittle and, as a result, a five-mile section was replaced in 2014 after being in service for only 40 years.[28]

Marion District supported the 40-year depreciable life assigned to mains installed after 2007 by explaining that switching from a 50-year life resulted in the write-off of $249,500 in additional depreciation, an amount that is significantly less than the $550,087 undepreciated cost of the 4,800 mechanical meters that Marion District has removed from service, but for which it has not recognized a loss by removing their undepreciated cost from its plant ledger. Marion District explained that the cost of these meters remain on its plant ledger and were depreciated during the test year using a 50-year life. Marion District stated that the "collective impact" of its decisions to not recognize the loss on the retired meters and to switch from a 50-year life to a 40-year life for mains installed after 2007 represents a "net conservative approach to depreciation expense for the District."[29]

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

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[28] Marion District's August 22, 2016 Response to Staff's Report at 2.

[29] *Id.*

1. Marion District was organized pursuant to KRS Chapter 74. It owns and operates a water distribution system through which it provides water service to approximately 5,900 customers in Marion County and Nelson County, Kentucky.[30] The calendar year ended December 31, 2015, should be used as the test year to determine the reasonableness of Marion District's existing and proposed water rates.

2. If during the test year Marion District had applied Staff's proposed method of accounting for employee retirement costs, Marion District would have first recorded the journal entries necessary to fully implement and account for the effects of GASB 68 on its financial statements[31] and it would have attached to its financial statements all the footnote disclosures required by GASB 68. It would have then made journal entries to reclassify as a Regulatory Asset the following items as allowed by GASB 62: a) the charge to retained earnings that was made to account for the cumulative effect of switching from GASB 27 to GASB 68; b) the Deferred Outflows and Deferred Inflows reported pursuant to GASB 68; and c) the difference between Marion District's retirement expense calculated pursuant to GASB 68 and its annual contributions to CERS.[32] Although footnote disclosure in Marion District's financial statements detailing the accounting for the pension Regulatory Asset pursuant to GASB 62 may not have been required, footnote disclosure would have been necessary to give the reader of the financial statements a clear understanding of Marion District's accounting for pensions.

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[30] Staff Report at 1.

[31] *Id.* at 21–22.

[32] *Id.* at 26.

3. If in each year subsequent to the test year Marion District follows Staff's method of accounting for pensions in accordance with GASB 62 and GASB 68, Marion District would make journal entries to: a) update the balance of the NPL to reflect the actuarial valuation for the year; b) record the Deferred Outflows and Deferred Inflows reported in the actuarial valuation; and c) record retirement expense as required by GASB 68. Marion District would then make all necessary journal entries to: a) reclassify to the Regulatory Asset account the current year's Deferred Outflows and Deferred Inflows related to pensions; b) reclassify to the Regulatory Asset account the difference between the GASB 68 pension expense and the contributions to CERS; and c) adjust Retained Earnings and the Regulatory Asset account by the amount necessary to restate the Regulatory Asset account's ending balance to an amount that is equal to the amount of NPL reported for the year. Marion District would make all the financial statement footnote disclosures required by GASB 68 as well as the footnote disclosures needed to explain its use of the Regulatory Asset account.

4. Staff's method does not "ignore GASB 68," as asserted by Marion District. Staff's method requires that Marion District recognize on its financial statements for the year ended December 31, 2015, and each year thereafter, its proportionate share of CERS's NPL in accordance with GASB 68.

5. Contrary to Marion District's claim, Staff's method addresses the reporting requirements that govern Marion District. GASB 62 is a part of the GASB accounting standards to which Marion District must adhere. GASB 62, Paragraph 480, states that:

> A regulated business-type activity should capitalize all or part of an incurred cost that otherwise would be charged to expense if both of the following criteria are met:
>
> a. It is probable that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for rate-making purposes.
>
> b. Based on available evidence, the future revenue will be provided to permit recovery of the previously incurred cost rather than to provide for expected levels of similar future costs.

The Regulatory Asset created pursuant to Staff's method of accounting for pensions satisfies the conditions of GASB 62. The amount of the NPL reported by Marion District for the test year represents the net present value of unfunded pension benefits that are payable to employees in return for services they provided during periods that occurred prior to the NPL's measurement date. These costs were first recognized in Marion District's financial statements as a charge against earnings during the test year pursuant to GASB 68. The prior period pension costs, or the NPL, will be funded by contributions to CERS that are made by Marion District in future reporting periods. Pursuant to Staff's method, these CERS contributions will be recovered through future rates, thus, fulfilling the requirements of GASB 62 and allowing the creation of the Regulatory Asset. The Regulatory Asset is equal to the amount of the NPL and is created by reversing the charge against earnings that was made by Marion District to implement GASB 68.

6. Finally, Marion District's concern that it cannot fund the CERS NPL without recovering through rates pension expense calculated pursuant to GASB 68, as requested in the Application, has no merit. The CERS NPL is funded through contributions received by CERS from its participating members. Pursuant to Staff's

method, Marion District will recover through rates the amounts it is required to contribute to CERS to fund the NPL.

7. Cavanaugh Macdonald Consulting, LLC ("CMC"), the preparer of the 2014 and 2015 CERS actuarial valuations, warned that significant fluctuations may occur in actuarial valuations from year-to-year due to "plan experience differing from that anticipated by the economic or demographic assumptions; changes in economic or demographic assumptions; increases or decreases expected as part of the natural operation of the methodology used from these measurements (such as the end of an amortization period or additional cost or contribution requirements based on the plans funded status); and changes in plan provisions or applicable law."[33]

8. The large fluctuations of which CMC warned occurred between the years 2014 and 2015. As previously discussed, using the 2014 actuarial valuation, Marion District calculated its test-year retirement expense to be $32,614, while Staff, using the 2015 actuarial valuation, determined the test-year expense to be $134,917.

9. It is reasonable to anticipate that large fluctuations in GASB 68 pension costs may occur in future years. Large fluctuations in the level of any expense may result in earnings reported from year-to-year that are erratic and should be avoided when permissible.

10. Pursuant to Staff's proposed method of accounting for GASB 68, Marion District's retirement expense will be equal to its contributions to CERS. Since the CERS contribution rates are historically constant, Staff's method will stabilize the amount of pension expense reported by Marion District from year to year, notwithstanding

[33] *Id.* at 16–17.

fluctuations that may occur due to changes in the level of Marion District's annual wages upon which the contributions are determined.

11. Staff's method of accounting for GASB 68 pension costs is in conformance with GASB's reporting requirements, is reasonable, and should be adopted by this Commission.

12. Although Marion District's implementation of GASB 68 using the 2014 actuarial valuation is in violation of Paragraph 48 of GASB 68, its use has no effect on the amount of Marion District's revenue requirement or its water service rates when Staff's method of accounting for pension costs is applied. Pursuant to Staff's method, Marion District's retirement expense for accounting and ratemaking purposes is $48,953, no matter which actuarial valuation is used. Therefore, Marion District's use of the 2014 actuarial valuation to report its test-year financial results to the Commission is acceptable.

13. Marion District is encouraged to record the journal entries in all future reporting periods to account for the pension Regulatory Asset account that results from Staff's method, but these entries are not required by this Order. If Marion District does not record these entries, Staff will determine the Regulatory Asset's account balance in each of Marion District's future rate case filings.

14. Marion District did not submit a depreciation schedule or plant ledger in Case No. 7901 to show the depreciable lives that had been assigned to its plant account groups in that proceeding; however, Charles M. White, CPA, testified that "the majority of lines are on a 2% depreciation," and that he did not develop the depreciation

rates, but rather he "inherited them," and he stated that "they won't let me change them."[34]

15. The Commission did not adjust the 2 percent depreciation rate in its final Order in that case and allowed Marion District to depreciate mains using a 50-year life. There is no evidence in the record of Case No. 7901 documenting the methods used by Marion District to select the 50-year life or the methods used by the Commission to determine its reasonableness. Consequently, there is no evidence from Case No. 7901 that can be made a part of this proceeding to support the 50-year life. The Commission is not bound by its Order in Case No. 7901 and may adjust the depreciable lives assigned to Marion District's main in this proceeding.

16. While the NARUC Study states that it is designed for small water utilities that have less than: 1) 200 customers; 2) $50,000 in annual revenue; and 3) $1,000,000 in plant investment, it further states that the average service lives of a small water utility would be similar to those of an average water utility when the small utility uses the same construction techniques and has similar equipment, maintenance standards, and accounting practices as the average utility.[35]

17. Since the depreciable lives in the NARUC Study are similar to those of an average utility, the NARUC Study may be used to evaluate the reasonableness of the depreciation practices of water districts and water associations regulated by the Commission without regard to the number of customers they serve or the amount of annual revenues and plant investment they report. The NARUC Study was used by the

[34] Case No. 7091, October 28, 1980 Hearing Transcript at 28–29. A 2 percent depreciation rate that does not include salvage represents a 50-year depreciable life (1 / .02 = 50).

[35] NARUC Study at iii–iv.

Commission as the basis for the depreciable lives authorized for Northern Kentucky Water District, the state's largest regulated water district serving over 100,000 customers and reporting over $50 million in annual revenues and over $468 million for utility plant.[36]

18. Although significant time has elapsed since its issuance, the NARUC Study represents a conservative estimate of the anticipated useful life of water mains that are constructed of either iron, PVC, galvanized steel, or concrete when compared to the results of the formal depreciation studies that have been approved by the Commission for Kentucky-American Water Company ("KAWC"), the only water utility that has routinely filed formal deprecation studies with the Commission. For example, in KAWC's most recent depreciation study approved by the Commission in Case No. 2015-00418,[37] the average service life assigned to the main account group, which included mains constructed of iron, PVC, galvanized steel, and concrete,[38] was 85 years, significantly longer than NARUC's 50 to 75 year life range. In that case, KAWC supported the 85-year life assigned to main, in part, by stating that this life was "within the typical service life range of 75 to 100 years for water mains,"[39] a life range that is significantly longer than the life range provided in the NARUC Study.

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[36] *See* Case No. 2006-00398, *Application of Northern Kentucky Water District for Approval of Depreciation Study* (Ky. PSC Nov. 21, 2007).

[37] Case No. 2015-00418, *Application of Kentucky-American Water Company for an Adjustment of Rates* (Ky. PSC Aug. 23, 2016).

[38] *Id.*, Application, Exhibit 10, Volume 1 of 2, Direct Testimony of Brent E. O'Neill, P.E., Exhibit BEO-1 at A-3.

[39] *Id.* Volume 2 of 2, Direct Testimony of John J. Spanos, Exhibit JJS-1 at III4.

19. It is appropriate to use the NARUC Study to evaluate the reasonableness of the depreciable lives assigned to Marion District's water plant account groups.

20. While some of Marion District's operating characteristics may be similar to those of Southern District, Marion District has not provided evidence demonstrating that its main overall have suffered the same level of accelerated decay as those of Southern District. While Marion District stated that it was required to replace five miles of PVC main due to decay after being in service for only 40 years, this main represents only 1.2 percent of Marion District's 436 total miles of main that were in service at the end of the test year.[40] Marion District has not provided evidence showing the cause of this decay or that this decay is pervasive throughout its distribution system.

21. The depreciable life assigned to a plant account group represents the anticipated average service life of all assets reported in the account group. Not all assets in the group are expected to remain in service for a period of time that is equal to the average life. Some assets will experience a shorter life while others will experience a longer life. Marion District's replacement of 1.2 percent of its mains after being in

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[40] *Annual Report of Marion County Water District to the Public Service Commission for the Calendar Year Ended December 31, 2015* at 62.

Water Main	
Diameter	Miles
12-Inch	12.63
8-Inch	19.81
6-Inch	96.39
4-Inch	124.16
3-Inch	179.66
2-Inch	3.13
Total	435.78

service for only 40 years does not warrant accelerating depreciation on all mains absent any evidence showing that a significant portion of those mains have also suffered from premature decay.

22. The depreciation of Marion District's mains should be independent of the accounting treatment applied to the undepreciated cost of the retired mechanical meters. Marion District should not "write-off" as a loss the undepreciated cost of the retired meters. Marion District may charge the undepreciated cost to Accumulated Depreciation following the accounting requirements of the Uniform Systems of Accounts.[41] This method of accounting would increase Marion District's depreciable basis in the new replacement meters by the amount of the undepreciated cost of the retired meters. In lieu of this method, Marion District may continue to report the cost of the retired meters on its plant ledger and depreciate their costs in future reporting periods as was done during the test year.

23. Marion District overstated, by a material amount, the undepreciated cost of the retired mechanical meters in its response to Staff's report. The $550,087 referenced by Marion District includes the cost of the mechanical meters as well as the cost to install those meters. Based on information provided by Marion District in Case No. 2003-00274, the Commission estimates the amount of the meters' cost that is

[41] USoA for Class A/B Water Districts and Associations at 42, 108.1, B.

included in the $550,087 referenced by Marion District is approximately $41,475.[42] If Marion District decides to remove the cost of the retired mechanical meters from its plant ledger, it should remove only the cost of the meters. The cost of the meter installations should not be removed because they remain in service as part of the new replacement meters.

24. There being no evidence in the record supporting a depreciable life for mains that is shorter or longer than the midpoint of the NARUC range, Marion District should depreciate water main using the midpoint, 62.5 years, in all future reporting periods.

25. After adjusting Marion District test-year operations for known and measurable changes, Marion District's total pro forma present rate revenues and total pro forma operating expenses are $2,668,954 and $2,573,564, respectively.[43]

26. Marion District currently has outstanding long-term debts payable to the United Stated Department of Agriculture Rural Development, Kentucky Infrastructure Authority, and Citizens National Bank. The five-year average principal and interest

[42] Case No. 2003-00274, *Application of Marion County Water District to Increase Certain Non-Recurring Charges* (Ky. PSC July 31, 2003). The cost information shown below was taken from the Average Meter Connection Expense Cost Justification sheet that was provided to the Commission by Marion District.

Cost of a 5/8-3/4-Inch Meter	$ 37.80
Divide by: Average Cost of a Meter and Meter Installation	501.34
Percent of Meter Cost to Total Cost	7.5398%
Times: Total Cost Reported by Marion District	550,087
Estimated Cost of Meters Reported by Marion District	$ 41,475

[43] Staff Report at 5. $2,503,565 (Water Sales Revenues) + $122,222 (Other Operating Revenue) + $3,704 (Interest Income) + $39,463 (Nonutility Income) = $2,668,954.

payments for the years 2017 through 2021 on these evidences of indebtedness is $145,253.[44]

27. The average annual debt payment that should be included in Marion District's Overall Revenue Requirement should be equal to the five-year average of the years 2017 through 2021. The five-year average allows Marion District recovery of the debt payments that will be made during the anticipated life of the rates authorized by the Commission herein.

28. The Commission has historically used a Debt Service Coverage ("DSC") method to calculate the revenue requirements of water districts with long-term debt.

29. Application of the Commission's DSC method to Marion District's pro forma operations results in an overall revenue requirement of $2,747,867. Revenue of $2,582,478 from water service rates is necessary to generate the overall requirement.[45]

30. The rates set forth in Appendix A to this Order will produce the required revenues, 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. The water service rates requested by Marion District are denied.

2. The water service rates set forth in the Appendix to this Order are approved for services rendered by Marion District on and after the date of this Order.

3. Within 20 days of the date of this Order, Marion District shall file revised tariff sheets with the Commission using the Commission's electronic Tariff Filing System containing the rates set forth in the Appendix of this Order.

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[44] *Id.* at 33–34.

[45] *Id.* at 33.

4. In all future reporting periods, Marion District shall depreciate its Water Transmission and Distribution Main account group using a 62.5-year depreciable life. No adjustment to accumulated depreciation or retained earnings should be made to account for this change in accounting estimate.

By the Commission

ENTERED

NOV 10 2016

KENTUCKY PUBLIC SERVICE COMMISSION

ATTEST:

Talina R. Mathews

Executive Director

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2016-00163 DATED NOV 10 2016

The following rates and charges are prescribed for the customers in the area served by Marion County 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

Customer Charge by Meter Size

Meter Size	Charge
5/8- x 3/4-Inch	$7.45
1-Inch	16.20
2-Inch	25.68
3-Inch	40.73
4-Inch	64.60
6-Inch	162.59

Water Charge

All Usage	5.65 per 1,000 gallons

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