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PUBLIC SERVICE
COMMISSION

Western Lewis Rectorville Water and Gas District
8044 KY 3160
Maysville, KY 41056

January 17, 2019

Public Service Commission
Attn: Gwen R. Pinson, Executive Director
PO Box 615
Frankfort, KY 40602-0615

RE: Western Lewis-Rectorville Water and Gas District
Case No. 2018-00321 - Response to PSC Staff Report dated January 7, 2019

Summary of Findings:

1. The District has taken into consideration and reviewed the changes made in the Staff Report to the Debt Service Calculation. However, after careful and thoughtful review of the changes made, the District has outlined various reasons and explanations throughout this response to reduce or eliminate several of those changes. While changes made to the Pro Forma Operating Statement noted in #2 below do lower our required revenue requirement to 42.20%, we are still asking for a 35.08% increase.

2. As with #1 above, the District has taken into consideration and reviewed the changes made in the Staff Report to the Pro Forma Operating Statement. As noted below in the Pro Forma Operating Statement section, the District does not agree with all of the adjustments made with reasons noted.

3. After review of the depreciable lives noted in item (F) under the Pro Forma Operating Statement section below, the District does not agree with the depreciable lives used. Please review item (F) below to understand the District's stance on the matter.

4. Thank you for recognizing the work the District put into making corrections previously noted by the Commission.

5. The District does not believe there are any problems with the new Automated Meter Reading (AMR) system. The new system reads water usage at the same intervals as the previous system. There are no calculations that are read to the 100-gallon mark, all are to the 1,000-gallon mark. Therefore, no revenue issues arise from the reading of the meters in 1,000-gallon increments. All customers are billed per 1,000 gallons used.

Pro Forma Operating Statement Responses and Adjustments:

Following is the Pro Forma Operating Statement as revised by the District, with explanations following:

	Test Year Operations	Reallocation Adjustments	Reallocated Operations	Pro Forma Adjustments	Adj. Ref.	Pro Forma Operations
Operating Revenues:						
Revenues from Water Sales	$ 813,191	$ (13,580)	$ 799,611	$ 50,095	(A)	$ 849,706
Other Operating Revenues	48,366	1,366	49,732			49,732
Total Water Operating Revenues	861,557	(12,214)	849,343	50,095		899,438
Operating Expenses:						
Operation and Maintenance Expenses:						
Salaries & Wages - Employees	231,474		231,474	(11,464)	(B)	220,010
Salaries & Wages - Commissioners	23,307		23,307			23,307
Emp. Pensions & Benefits	69,696		69,696	18,462	C	88,158
Purchased Water	71,163		71,163	(1,825)	(D)	69,338
Purchased Power	42,212	9,405	51,617	(1,337)	(D)	50,280
Chemicals and Water Testing	12,233	2,725	14,958	(387)	(D)	14,571
Materials and Supplies	110,557		110,557	-	(B)	110,557
Contractual Services	52,970		52,970			52,970
Rental Equipment	207		207			207
Insurance	92,578		92,578	(44,131)	E	48,447
Miscellaneous	19,449		19,449			19,449
Total Operation & Maint Exp	725,846	12,130	737,976	(40,682)		697,294
Depreciation and Amortization	339,305		339,305	(36,710)	(F)	302,595
Taxes Other Than Income Tax	20,335		20,335	(772)	(G)	19,563
Total Water Operating Expenses	1,085,486	12,130	1,097,616	(78,164)		1,019,452
Net Operating Income	(223,929)	(24,344)	(248,273)	128,259		(120,014)
Other Income & Deductions:						
Nonutility Income	39,395		39,395	(25,554)	(H)	13,841
Net Income Available for Debt Service	$ (184,534)	$ (24,344)	$ (208,878)	$ 102,705		$ (106,173)

(A) While reviewing revenues to determine why there was such a large variance between normalized revenues and actual revenues for the test year we found the following explanations. First, the billing analysis prepared in the application calculates the amount of the water bills issued to customers without regard to amounts that will actually be collected. While the District does collect a large percentage of the billed revenues, not all can be expected to be received. Second, on a purely cash basis the District collected and posted $834,281 to the water collections general ledger line item. Only after accrual journal entries to prepare GAAP financial statements did the water collections then reflect a balance of $799,611 on the general ledger. In order to match the PSC Annual Report and the Audit Report the $813,191 was used on the application to reflect Revenue from Water Sales. Therefore, if we take the difference between the normalized revenue and the actual revenues collected there is only a difference of $30,425. We understand that there has to be a calculation of normalized revenue, however, it cannot be expected that all amounts billed will be collected. We would like the Commission to consider reducing the amount of normalized revenues by $15,000 to $849,706.

(B) Employees salaries and wages were reduced by the vacant employee wages, as well as employee vacation payout and capitalized wages. We will agree to the first two, however, not the reduction for capitalized wages. The new taps for water were put in as part of the construction project. Therefore, the materials and labor were both provided by the construction company and capitalized as part of the completed project. Therefore, we will add back $11,250 to both the materials and supplies, as well as the employees salaries expense. We will also remove the depreciation expense of $549 used in the calculation of F below.

(C) Health insurance was combined with the line item insurance expense, not employee benefits. This is because on the audit report the line item is not employee benefits, but retirement expense. While we do not agree that the amount of health insurance the district agrees to pay for should be adjusted, we will accept the revised calculation for employee benefits.

(D) We do not agree that the purchased water, power, or chemicals should be reduced to the extent noted in the staff report. In reference to the excess water calculation we do not agree with how the system flushing adjustment was calculated. Chad Clark, District Manager, agreed that with the new filters in place at the plant the water produced and used at the treatment plant would essentially be eliminated. However, the system will still have to be flushed, but the process will only use about half as much water as in prior years. Like the elimination of water produced relating to the utility/water treatment adjustment for usage, water produced would also be reduced by the same amount as the adjustment for system flushing. Please see the "Staff Adjustment – Revised" column below for the noted changes. As the revised calculation shows, the excess water loss percentage is reduced from 11.38% to 2.59%.

		Actual	Staff Adjustment Revised	Adjusted
Water Produced		113,110,000	(15,025,000)	98,085,000
Water Purchased		32,676,000	-	32,676,000
Test-Year Water Produced/Purchased		145,786,000	(15,025,000)	130,761,000
Less:	Volume Sold During Test Year	(100,481,000)	(410,000)	(100,891,000)
	Utility/Water Treatment Plant	(8,400,000)	8,400,000	-
	System Flushing	(13,250,000)	6,625,000	(6,625,000)
	Fire Department	(250,000)	-	(250,000)
Water Loss		23,405,000	(410,000)	22,995,000
Divide by:	Water Produced/Purchased	145,786,000		130,761,000
Percent Loss		16.05%		17.59%
Allowable Water Loss		-15.00%		-15.00%
Excess Water Loss Percentage		1.05%		2.59%

With the revised excess water loss percentage noted above, following is the revised pro forma expenses:

	Chemicals	Purchased Power	Purchased Water
Pro Forma Subject to Water Loss Adjustment	$ (14,958)	$ (51,617)	$ (70,479)
Tims:Water Loss in Excess of 15%	2.59%	2.59%	2.59%
Pro Forma Water Loss Adjustment	$ (387.41)	$ (1,336.88)	$ (1,825.41)

(E) As noted in C above, health insurance was included in the insurance expense line item. Thus, we will agree to a reduction of expenses, but we do not agree to the extent listed. Liability insurance (both general and property) are covered under the KLC Premium Finance Company Inc. The policy premium payments are broken down to a 20% down payment and 9 installment payments. During 2017 payments to KLC Premium Finance Company totaled $54,846. Additionally, the worker's compensation audit premium was $585. The last item included in insurance expense is the annual surety bond for employees for which the District paid $3,385 during 2017. We will use the allocation factor of 90.53% for workers compensation and surety bond and 81.78% for the liability premiums. Thus, the actual expense would be $48,447 (($585 + $3,385) * 90.53% + $54,846 * 81.78%), which is a decrease of $44,131.

(F) It was noted in the staff report "...that all of Western Lewis-Rectorville District's asset categories are outside of the ranges in the NARUC Study". However, upon review of the table, that does not appear to be the case. Most asset categories match, or exceed, the floor depreciable life as noted in the NARUC Study. Furthermore, the one asset classification with the bulk of the cost, Transmission & Distribution Mains, is within less than 7 years of the 50-year floor range.

Although the Commission has historically used the mid-point of the NARUC range, we believe it would be more reasonable to use the floor of the NARUC range, as it is more in line with what the District already has in place. If this is agreed to by the Commission, we will change our depreciable lives on any new assets added in the future. We will also recalculate annual depreciation for 2018 and future, where necessary, on any assets with useful lives not already at the floor. For the purpose of determining the adjustment to the pro forma operating statement we have made the following calculation:

						NARUC Depreciation Lives			Staff - Revised	
	Original Cost UPIS	Dep. Life	Accum. Dep. 2016	Dep. Exp. 2017	Accum. Dep. 2017	Floor	Ceiling	Mid-Point	Dep. Expense	Pro Forma Adjustment
Structures and Improvements	465,619	36.60	3,312	12,723	16,035	35.00	40.00	37.50	12,723	-
Wells & Springs	94,304	25.00	29,801	3,632	33,433	25.00	35.00	30.00	3,632	-
Pumping Equipment	9,793	20.00	8,665	149	8,814	20.00	20.00	20.00	149	-
Distribution Reservoirs & Standpipes	1,045,463	30.00	450,506	34,849	485,355	30.00	60.00	45.00	34,849	-
Transmission & Distribution Mains	10,537,119	43.57	3,500,927	241,826	3,742,753	50.00	75.00	62.50	210,742	(31,084)
Meter	197,560	10.00	97,889	19,756	117,645	35.00	50.00	42.50	5,645	(14,111)
Office Equipment	62,727	10.00	3,437	6,273	9,710	20.00	25.00	22.50	3,136	(3,137)
Transportation Equipment	31,363	5.00	12,545	6,273	18,818	7.00	7.00	7.00	4,480	(1,793)
Other Tangible Plant	134,139	10.00	32,104	13,414	45,518	5.00	5.00	5.00	26,828	13,414
Power Operated Equipment	4,056	10.00	3,650	406	4,056	5.00	5.00	5.00	406	-
Pro Forma Adjustment	12,582,143		4,142,836	339,301	4,482,137				302,591	(36,710)

(G) As noted in B above, we did not agree with all of the changes to employee wages. Additionally, the Commissioners salaries should have also been taken into account when calculating FICA. Therefore, our revised calculation for FICA is $18,614 (($220,010 + $23,307) * 7.65%). In addition to FICA, the District is required to pay Kentucky Unemployment. In 2017 that amount totaled $1,048 for the entire year. Pro-rated for only water at 90.53% the amount would be $949 of additional employer payroll taxes. Total FICA and unemployment totals $19,563, which is only a $772 decrease from the original amount reported.

Overall Revenue Requirement and Required Revenue Increase

		District	Staff - Revised	
Pro Forma Operating Expenses		$ 1,085,486	$ 1,019,452	
Plus:	Average Annual Debt Principal and Interest Payments	210,326	210,326	(I)
	Debt Coverage Requirement	-	42,065	(I)
Total Revenue Requirement		1,295,812	1,271,843	
Less:	Other Operating Revenue	(48,366)	(49,732)	
	Non-Operating Revenue	(486)	(13,841)	(H)
Revenue Required from Rates		1,246,960	1,208,270	
Less:	Normalized Revenues from Water Sales	(813,191)	(849,706)	(A)
Required Revenue Increase/(Decrease)		$ 433,769	$ 358,564	
Percentage Increase		53.34%	42.20%	

(H) Non-Operating Revenues: Non-operating revenues were reported at $39,395, however of that total $25,554 was related to the gain on sale/disposal of assets. This is not a normal recurring income and as such, should not be included when determining future revenues. Due to this explanation we will calculate non-operating income at $13,841.

) Average Annual Principal and Interest Payments: We do not agree with the change to the average annual debt principal and interest payments. As can be shown in the audit report the three years of debt service payments are as follows:

	Debt Service FmHA/RD	Debt Service KIA	Total Debt Service
2018	$ 162,638	$ 47,818	$ 210,456
2019	162,719	47,818	210,537
2020	162,167	47,818	209,985
3-Year Average			$ 210,326

Therefore, we will use the $210,326 for the Average Annual Debt Principal and Interest Payments in the calculation. We agree that we need to include the 1.2x debt coverage requirement and have calculated that at $42,065 ($210,326*.2).

The information was provided by Chad Clark, General Manager, Pauline Calhoun, Sr. Office Clerk, and yn Rhonemus, CPA. The information provided is true and accurate to the best of our knowledge, information and belief formed after a reasonable inquiry.

Chad Clark
Chad Clark, General Manager

01/17/2019
Date

Pauline Calhoun
Pauline Calhoun, Sr. Office Manager

1-17-2019
Date

Lyn Rhonemus
Lyn Rhonemus, CPA

01/17/19
Date