

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF MORGAN COUNTY WATER) CASE NO.
DISTRICT FOR RATE ADJUSTMENT) 2016-00068

ORDER

By this Order, the Commission approves an increase to Morgan County Water District's ("Morgan District") water service rates. The approved water rates will generate \$165,260 in additional annual revenues, a 14.97 percent increase to pro forma present water rate revenues in the amount of \$1,103,939. The monthly water bill of a typical residential customer¹ will increase from \$45.75 to \$52.60, an increase of \$6.85, or 14.97 percent.

On February 4, 2016, Morgan District tendered an application ("Application") to the Commission pursuant to 807 KAR 5:076 requesting to increase its water service rates by 14.97 percent. After deficiencies were cured, the Application was accepted for filing as of April 21, 2016. To ensure the orderly review of the Application, the Commission issued a procedural Order on May 5, 2016, requiring Commission Staff ("Staff") to prepare and file a report containing its findings regarding the rate increase requested in the Application. The Order required that all parties file comments or objections to Staff's findings. The Order stated that a party's failure to file an objection to a finding would be deemed as a waiver of all objections to the finding.

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

On July 11, 2016, Staff issued a report summarizing its findings (“Report”). Staff found that Morgan District’s adjusted test-year operations support a 26.56 percent water service rate increase. The water rates calculated by Staff were presented in Attachment A of Staff’s Report.

On August 1, 2016, Morgan District filed with the Commission its comments on Staff’s Report wherein it requested that the Commission authorize the 14.97 percent water rate increase originally requested in the Application. It did not object to any of Staff’s findings. Morgan District did not request that a conference or hearing be held.²

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

1. Morgan District, a water district organized pursuant to KRS Chapter 74, owns and operates a water distribution system through which it provides retail water service to approximately 2,650 customers in Morgan County, Kentucky.
2. The calendar year ended December 31, 2014, should be used as the test period to determine the reasonableness of Morgan District’s water service rates.
3. Based upon pro forma test-year operations, after adjusting for known and measurable changes, Morgan District’s pro forma present rate revenues and total pro forma operating expenses are \$1,151,348³ and \$1,164,471,⁴ respectively.
4. Morgan District has nine outstanding bond issuances that are payable to the United States Department of Agriculture Rural Development (“RD”). The five-year

² Letter from Roy Collett, Chairman, Morgan County Water District, to Jeff Derouen, former Executive Director, Public Service Commission (Aug. 1, 2016).

³ Staff’s Report at 4. \$1,103,939 (Revenue from Water Sales) + \$47,062 (Other Water Revenues) + \$347 (Interest and Dividend Income) = \$1,151,348.

⁴ *Id.*

average annual principle and interest payment on all debts for the years 2017 through 2021 is \$233,388.⁵

5. The Commission has historically used a Debt Service Coverage (“DSC”) method to calculate the revenue requirement for water districts or associations with outstanding long-term debt.

6. Application of the Commission’s DSC method to Morgan District’s pro forma operations results in an Overall Revenue Requirement in the amount of \$1,444,537. A revenue increase of \$293,189 from water service rates is necessary to generate the overall revenue requirement.⁶

7. The water service rates requested by Morgan District in the Application and in its August 1, 2016 response to Staff’s Report will not produce \$293,189 in additional annual revenues. The rates requested by Morgan District will produce

⁵ *Id.* at 21.

⁶ *Id.* at 17.

\$165,260 in additional annual revenues, which is sufficient for Morgan District to meet the DSC ratio requirement of RD, Morgan District's lender.⁷

8. The record contains no evidence that permitting Morgan District to assess the requested water service rates will result in any degradation or reduction in the quality of sewer service currently provided by Morgan District.

9. A utility may assess rates that fail to produce a level of revenues that accepted ratemaking methodologies would regard as sufficient or adequate. Absent evidence that the quality of the utility's service will decline or be degraded as a result of

⁷ RD requires Morgan District to assess water service rates that will generate net revenues that are equal to at least 120 percent of Morgan District's average annual bond payments. As shown below, the rates requested by Morgan District will generate net revenues that produce a DSC Ratio of 154.31 percent, which is above RD's minimum requirement.

Pro Forma Present Rate Revenues	\$ 1,103,939
Plus: Additional Annual Revenues from Requested Rates	165,260
Other Operating Revenues	47,062
Interest Income	<u>347</u>
 Total Revenue	 1,316,608
Less: Pro Forma Operation and Maintenance Expenses	(809,394)
Cost of Excess Water Loss Eliminated for Rate Making Purposes (includes Purchased Water and Purchased Power)	(134,743)
Taxes Other Than Income Taxes	<u>(12,328)</u>
 Net Revenues Upon which DSC Ratio is Calculated	 360,143
Divide by: Average Annual RD Debt Payments	<u>233,388</u>
 DSC Ratio	 <u>154.31%</u>

this level of revenue, the water service rates requested by Morgan District should be approved by the Commission.⁸

10. Except for the portion of Morgan District's telemetry system that was placed into service during the year 2010, Morgan District recorded the original cost of all water plant assets that had not been fully depreciated as of the end of the test year using the "Water Lines" plant subsidiary account. Morgan District applied a 50-year depreciable life to the cost of all assets reported to the "Water Lines" account to calculate test-year depreciation.⁹

11. The assets that Morgan District has recorded as "Water Lines" include structures and Improvements, water transmission and distribution main, water storage tanks, pumping stations, bulk loading stations, meter installations, valves, and hydrants.¹⁰ The cost of each of these assets should be reported separately in Morgan District's plant ledger using the appropriate plant subsidiary accounts that are prescribed by the Uniform System of Accounts ("USoA") as shown in Appendix B.¹¹ The cost appropriately recorded to each USoA plant subsidiary account should then be depreciated for ratemaking and accounting purposes in all future reporting periods using practices that are generally accepted by the Commission.

⁸ *Utilities Operating Co. v King*, 143 So.2d 854, 45 PUR3d 439, 443 (Fla. 1962) ("[I]n the absence of some showing that the service to the public will suffer by allowing the utility to charge rates which will not produce a fair return, the utility and not the Commission has the right of decision as to the rates it will charge so long as they do not exceed those which would produce a fair return as determined by the Commission."). See also Case No. 2006-00410, *The Application of Hardin County Water District No. 1 for a General Rate Adjustment Effective on and after December 2, 2006* (Ky. PSC Aug. 2, 2007); and Case No. 98-398, *Adjustment of Rates of the Kentucky Turnpike Water District and the Imposition of an Impact Fee* (Ky. PSC June 30, 1999).

⁹ Staff's Report at 11.

¹⁰ *Id.* at 10.

¹¹ Uniform System of Accounts for Class A/B Water Districts and Associations ("USoA") at 64–79.

12. The National Association of Regulatory Utility Commissioners (“NARUC”) has published a depreciation manual (“NARUC Manual”) that contains “a range of average service lives currently being used by water utilities throughout the country for water facilities designed and installed and maintained in accordance with good water works practice.”¹²

13. The Commission has previously used the NARUC Manual to establish the service lives of water assets when there is no evidence in the record to support alternative lives.¹³

14. Staff found that Morgan District’s water plant assets should be depreciated using the longest lives shown in the NARUC Manual.¹⁴ Morgan District did not object to Staff’s finding.

15. Morgan District’s assignment of test-year depreciable lives should be revised for ratemaking and accounting purposes in all future reporting periods as found appropriate by Staff and shown in Appendix C of this Order.

16. Morgan District’s test-year water loss was 38.83 percent, or 23.83 percent higher than the 15 percent allowed for ratemaking purposes pursuant to 807 KAR 5:066, Section 6(3).¹⁵ The cost to Morgan District to purchase and pump the excess

¹² National Association of Regulatory Utility Commissioners, *Depreciation Practices for Small Water Utilities* (Aug. 15, 1979) at 11.

¹³ Case No. 2006-00398, *Application of Northern Kentucky Water District for Approval of Depreciation Study* (Ky. PSC Nov. 21, 2007); and Case No. 2012-00278, *Application of Graves County Water District for an Adjustment in Rates Pursuant to the Alternative Rate Filing Procedure for Small Utilities* (Ky. PSC Sept. 5, 2012).

¹⁴ Staff’s Report at 14.

¹⁵ Staff’s Report at 8.

water lost is approximately \$134,273,¹⁶ an amount that is significant. The Commission is concerned with excessive water loss and related costs and directs Morgan District to develop and formally adopt a written plan to reduce excessive water loss. The plan should identify all sources of water loss and each corrective action Morgan District will take to minimize water loss from each source.

IT IS THEREFORE ORDERED that:

1. The monthly water service rates requested by Morgan District in the Application and in its August 1, 2016 response to Staff's Report are approved.

2. Morgan District shall charge the water service rates that are set forth in Appendix A for water service rendered on and after the date of this Order.

3. Morgan District shall make adjusting journal entries to its plant ledger that are necessary to reclassify the original cost of plant, and of depreciation that had accumulated thereon as of the end of the test year, to the appropriate plant subsidiary accounts as shown in Appendix B of this Order. Any depreciation that has accrued on these assets since the end of the test year shall be allocated to each plant subsidiary account based on the account's percentage of accumulated depreciation test-year-end depreciation when compared to the accumulated depreciation at test-year-end for all accounts. These percentages are also shown in Appendix B.

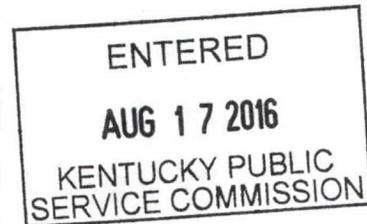
4. Morgan District shall use the "PSC Approved Service Life" set forth in Appendix C to depreciate water plant assets for ratemaking and accounting purposes in all future reporting periods. No adjustment shall be made to accumulated depreciation or retained earnings to account for this change in accounting estimate.

¹⁶ *Id.* at 9.

5. Within 20 days of the date of this Order, Morgan District shall file revised tariff sheets with the Commission, using the Commission's electronic Tariff Filing System, setting forth the water service rates approved herein.

6. Within 90 days of the date of this Order, in accordance with finding paragraph 16, Morgan District shall file with the Commission a copy of its excessive water loss reduction plan and a copy of the minutes from its Board of Commissioners' meeting where the plan was adopted.

By the Commission



ATTEST:

A handwritten signature in blue ink that reads "Jalina R. Mathews". The signature is written in a cursive style and is positioned above a horizontal line.

Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2016-00068 DATED **AUG 17 2016**

The following water service rates and charges are prescribed for the water customers in the area served by Morgan 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

5/8- x 3/4-Inch Meter

First	2,000 gallons	\$ 25.00	Minimum bill
Next	3,000 gallons	9.20	per 1,000 gallons
Next	5,000 gallons	8.51	per 1,000 gallons
Next	5,000 gallons	7.82	per 1,000 gallons
Over	15,000 gallons	7.13	per 1,000 gallons

1-Inch Meter

First	5,000 gallons	\$ 52.73	Minimum bill
Next	5,000 gallons	8.51	per 1,000 gallons
Next	5,000 gallons	7.82	per 1,000 gallons
Over	15,000 gallons	7.13	per 1,000 gallons

2-Inch Meter

First	15,000 gallons	\$ 133.23	Minimum bill
Over	15,000 gallons	7.13	per 1,000 gallons

6-Inch Meter

First	100,000 gallons	\$ 740.31	Minimum Bill
Over	100,000 gallons	7.13	per 1,000 gallons

Wholesale User Rates

City of Campton	\$ 4.05	per 1,000 gallons
City of Frenchburg	\$ 4.05	per 1,000 gallons

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
 COMMISSION IN CASE NO. 2016-00068 DATED **AUG 1.7 2016**

Test-Year Ending Balances for Plant
 Subsidiary Accounts by Vintage

<u>Plant Subsidiary Account</u>	<u>Allocated Cost</u>	<u>Allocated Accumulated Depreciation</u>
Structures and Improvements		
1993	\$ 36,388	\$ 14,192
1996	28,736	11,207
1998	18,000	15,302
1999	31,657	10,183
2000	9,235	2,809
2002	412,022	107,735
2006	207,974	37,971
2008	231,918	36,359
2010	300,789	33,619
	<u>1,276,719</u>	<u>269,377</u>
Pumping Equipment		
2002	<u>10,049</u>	<u>2,628</u>
Distribution Reservoirs and Standpipes		
1996	218,595	85,252
2006	430,826	78,658
2010	533,099	59,023
	<u>\$ 1,182,519</u>	<u>\$ 222,933</u>

<u>Plant Subsidiary Account</u>	<u>Allocated Cost</u>	<u>Allocated Accumulated Depreciation</u>
Transmission and Distributions Mains		
1989	\$ 1,060,000	\$ 500,993
1993	718,872	280,360
1996	996,225	388,528
1999	224,568	72,236
2000	65,509	19,926
2002	1,939,158	507,050
2003	1,722,021	416,210
2006	3,052,866	557,378
2008	3,023,832	474,064
2010	2,814,009	310,170
	<u>15,617,059</u>	<u>3,526,915</u>
Meters and Meter Installations		
1993	17,737	6,917
1999	19,501	6,273
2000	5,689	1,730
2002	254,580	66,567
2006	514,957	94,018
2008	784,648	123,014
2010	231,936	25,575
	<u>1,829,047</u>	<u>324,095</u>
Hydrants		
1999	9,497	3,055
2000	2,770	843
2002	38,407	10,043
2006	21,407	3,908
2008	33,210	5,207
2010	69,542	7,742
	<u>174,835</u>	<u>30,797</u>
Communication Equipment		
1996	30,513	11,900
2002	48,420	12,661
	<u>78,933</u>	<u>24,561</u>
Total for all Accounts	<u>\$ 20,169,161</u>	<u>\$ 4,401,305</u>

APPENDIX C

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2016-00068 DATED **AUG 1, 7 2016**

Modifications to the Depreciable Lives of Certain
Assets of Morgan County Water District

<u>Plant Subsidiary Account</u>	<u>Depreciable Life</u>		
	<u>Used By Morgan District</u>	<u>NARUC Range</u>	<u>PSC Approved</u>
Structures and Improvements	50	35-40	40
Pumping Equipment	50	20	20
Reservoirs and Standpipes	50	30-60	60
Transmission and Distribution Main	50	50-75	75
Meters and Meter Installations	50	35-50	50
Hydrants	50	40-60	60
Communication Equipment			
2010 Telemetry	10	10	10
All Other	50	10	10

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