

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

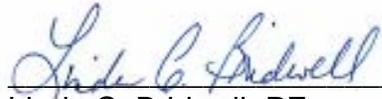
In the Matter of:

ELECTRONIC APPLICATION OF ALLEN)	CASE NO.
COUNTY WATER DISTRICT FOR AN)	2020-00296
ALTERNATIVE RATE ADJUSTMENT)	

NOTICE OF FILING OF COMMISSION STAFF REPORT

Notice is hereby given that, in accordance with the Commission's Orders of October 13 2020, the attached report containing the findings of Commission Staff (Staff) regarding the Applicant's proposed rate adjustment has been filed in the record of the above-styled proceeding. Pursuant to the Commission's October 13, 2020 Order, Allen County Water District (Allen District) is required to file written comments regarding the findings of Staff no later than 14 days from the date of this report. Pursuant to the Commission's Orders in Case No. 2020-00085,¹ issued March 16, 2020, and March 24, 2020, Allen District SHALL NOT FILE the original paper copy of its comments at this time, but rather shall file original paper copies within 30 days of the lifting of the current state of emergency. Due to COVID-19, Staff is unable to physically sign this report. When Staff is able to safely sign this report, a notice of filing with the executed signature page will be made in this case docket.

¹ Case No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19* (Ky. PSC Mar. 16, 2020), Order at 5–6. Case No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19* (Ky. PSC Mar. 24, 2020), Order at 1–3.



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

DATED DEC 16 2020

cc: Parties of Record

Case No. 2020-00296

STAFF REPORT
ON
ALLEN COUNTY DISTRICT
CASE NO. 2020-00296

Allen District is a water utility organized pursuant to KRS Chapter 74 that owns and operates a water distribution system through which it provides retail water service to approximately 5,809 retail customers, and one wholesale customer, that reside in Allen County, Kentucky.¹ In the final Order for case 2019-00398, Allen District was ordered to request to adjust its rates for water service pursuant to 807 KAR 5:076 no later than July 1, 2020.² On September 18, 2020, Allen District tendered an application to the Commission requesting to adjust its water rates pursuant to 807 KAR 5:076. To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated October 13, 2020. Staff issued its first round of formal discovery on October 14, 2020, a second round of formal discovery on November 9, 2020, and a final round of formal discovery on December 1, 2020.

The Commission notes in its 2019 Annual Report that Allen District reported a water loss of 30.8998 percent.³ Commission regulation 807 KAR 5:066(6)(3) states that for rate making 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.

¹ *Annual Report of Allen District to the Public Service Commission for the Calendar Year Ended December 31, 2019 (Annual Report)* at 12 and 49.

² See Case No. 2019-00398, *Application of Allen County Water District for the Issuance of a Certificate of Public Convenience and Necessity to Construct a Water System Improvements Project and an Order Authorizing the Issuance of Securities Pursuant to the Provisions of KRS 278.020, KRS 278.300, and 807 KAR 5:001* (Ky. PSC Dec. 19, 2019).

³ *Annual Report* at 57.

Reduction of Allen District’s water loss to 15 percent would result in an approximate \$112,842⁴ decrease to purchased water expense. Potentially, Allen District is paying \$0.08 per 1,000 gallons sold, for expenses associated with water loss greater than 15 percent.⁵

The Commission is placing greater emphasis on monitoring utilities that consistently exceed the 15 percent water loss threshold and strongly encourages Allen District to pursue reasonable actions to reduce its water loss. Failure by Allen District to make significant progress towards reducing water loss may cause the Commission to pursue additional action with the utility.

To comply with the requirements of 807 KAR 5:076, Section 9,⁶ Allen District used the calendar year ended December 31, 2019, as the basis for its application. Using its Pro Forma test-year operations, Allen District determined that a revenue increase of \$369,531, or 15.8 percent, over test-year normalized revenues of \$2,343,426 is warranted as shown in the table below.⁷ The rates requested by Allen District would

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	Purchased Water from 2019 Annual Report	\$ 709,705
	Times: Water loss Above 15 Percent	<u>15.9%</u>
	Purchased Water Expense Reduction	\$ 112,842

⁵ Potential purchased water expense reduction divided by sales (\$112,842/(1,470,733/1,000) equals \$0.08 per 1,000 gallons.

⁶ The reasonableness of the proposed rates shall be determined using a 12-month historical test period, adjusted for known and measureable changes, that coincides with the reporting period of the applicant’s annual report for the immediate past year.

⁷ Application, Attachment 5.

increase the residential monthly bill of a typical residential customer using 4,000 gallons per month by \$5.45, from \$34.45 to \$39.90, or approximately 15.8 percent.⁸

<u>Revenue Requirement Determination- Debt Service Method</u>	
Pro Forma Operating Expenses	\$ 2,326,148
Plus: Average Annual Principal and Interest Payments	474,621
Additional Working Capital	<u>94,924</u>
Overall Revenue Requirement	2,895,694
Less: Other Operating Revenue	(97,955)
Interest Income	(75,875)
Net nonutility Income	<u>(8,907)</u>
Revenue Required from Rates	2,712,957
Less: Pro Forma Present Rate Service Revenues	<u>(2,343,426)</u>
Required Revenue Increase	<u>\$ 369,531</u>
Percentage Increase	<u>15.8%</u>

To determine the reasonableness of the rates requested by Allen District, Staff performed a limited financial review of Allen District’s test-year operations. The scope of Staff’s review was limited to determining whether operations reported for the test year were representative of normal operations. Known and measurable changes to test-year operations were identified and adjustments made when their effects were deemed material. Insignificant and immaterial discrepancies were not necessarily pursued or addressed.

Staff’s findings are summarized in this report. William Foley reviewed the calculation of Allen District’s Overall Revenue Requirement. Eddie Beavers reviewed Allen District’s reported revenues and rate design.

⁸ *Id.*, Attachment 1.

SUMMARY OF FINDINGS

1. Overall Revenue Requirement and Required Revenue Increase. By applying the Debt Service method, as generally accepted by the Commission, Staff found that Allen District's required revenue from rates is \$2,611,200 to meet the Overall Revenue Requirement, representing a \$2,760,639 or 11.4 percent revenue increase to Pro Forma present rate revenues.

2. Monthly Water Service Rates. Allen District proposed to increase all of its monthly retail water service rates evenly across the board by approximately 15.8 percent. Allen District has not performed a cost of service study (COSS). In response to Staff's First Request for Information (Staff's First Request), Allen District stated that it did not complete a COSS at this time as there has not been any material change in the water system to warrant a COSS.⁹

The Commission has previously found that the allocation of a revenue increase evenly across the board to 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, Staff followed the method proposed by Allen District and allocated the \$267,773 revenue increase across the board to Allen District's monthly retail and wholesale water service rates.

The rates set forth in the Appendix to this report are based upon the revenue requirement, as calculated by Staff, and will produce sufficient revenues from water sales to recover the \$2,611,200 Revenue Required from Rates, an approximate 11.4 percent

⁹ Staff's First Request for Information (filed Oct. 28, 2020), Item 3.

increase. These rates will increase a typical residential customer's monthly water bill from \$34.45 to \$38.38, an increase of \$3.93, or approximately 11.4 percent.¹⁰

PRO FORMA OPERATING STATEMENT

Allen District's Pro Forma Operating Statement for the test year ended December 31, 2019, as determined by Staff, appears below.

	Test Year	Adjustment	(Ref.)	Pro Forma
Operating Revenues				
Total Retail Meter Sales	\$ 2,280,366	\$ (785)	(A)	\$ 2,279,581
Sales for Resale	-	63,846	(A)	63,846
Other Water Revenues				
Forfeited Discounts	50,093			50,093
Misc. Service Revenues	146,382	(98,520)	(B)	
		(33,298)	(C)	14,564
Other Water Revenues	49,975	(49,975)	(D)	-
Total Operating Revenues	\$ 2,526,816	\$ (118,732)		\$ 2,408,084
Operating Expenses				
Operation and Maintenance Expenses				
Salaries and Wages - Employees	529,451	(68,530)	(E)	
		(29,556)	(B)	431,365
Salaries and Wages - Officers	39,715	(9,715)	(G)	30,000
Employee Pensions and Benefits	277,930	221	(F)	
		(32,087)	(H)	246,064
Purchase Water	709,705	(112,842)	(I)	596,863
Purchased Power	65,964	(10,488)	(I)	55,476
Materials and Supplies	152,847	(68,964)	(B)	83,883
Contractual Services	167,929			167,929
Rental of Bldg/Property & Equipment	4,682			4,682
Transportation Expense	51,052			51,052
Insurance- Gen. Liability	17,038			17,038
Insurance- Workers Comp.	8,581			8,581
Insurance- Other	7,546			7,546
Miscellaneous Expense	23,104			23,104
Total Operation and Maintenance Expenses	2,055,544			1,723,583
Depreciation	546,044	(115,022)	(J)	
		2,318	(B)	433,340
Taxes Other Than Income	39,414	(5,243)	(K)	34,171
Total Operating Expenses	2,641,002	(117,947)		2,191,094
Net Utility Operating Income	(114,186)	(785)		216,990
Non Utility Income	86,723	(77,816)	(L)	8,907

¹⁰ The typical residential customer uses approximately 4,000 gallons per month.

(A) Billing Analysis Adjustment. Allen District proposed to decrease its test-year revenues from water sales of \$2,280,366 by \$785 to reflect the current billing analysis provided by the district. Allen District also made a similar adjustment for the wholesale water sales of \$63,846. Staff finds that Allen District’s adjustment meets the ratemaking criteria of being known and measurable and accepts both in Pro Forma operations.

(B) Tap-Ons. In its application, Allen District proposed adjustments to reduce Misc. Service Revenues by \$98,520, test-year labor by \$29,556, and materials and supplies by \$68,964 to correctly remove, for ratemaking purposes, revenues from tap-on fees as well as associated capital expenses from test-year operations.¹¹ Staff finds that Allen District’s adjustment meets the ratemaking criteria of being known and measurable and Staff accepts Allen District’s adjustment. In addition, Staff has capitalized the costs and made a corresponding adjustment increasing depreciation by \$2,318 to test-year depreciation as shown below.

Labor Expense Associated with Tap Ons	\$ 29,556
Materials and Supplies Expense Associated with Tap Ons	<u>68,964</u>
Test Year Tap On Expenses	98,520
Divided by: Useful Life of 42.5 Years	<u>42.5</u>
Pro Forma Depreciation Adjustment	<u><u>\$ 2,318</u></u>

(C) Nonrecurring Charges. Following the Commission’s recent decisions Hyden-Leslie Water District’s (Hyden-Leslie District) and Ohio County Water District’s

¹¹ Application, Attachment 5, Adjustments C and E.

recent Alternative Rate Filing (ARF),¹² Staff has reviewed Allen District’s nonrecurring charges. The Commission found that as district 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. Staff has reviewed the most recent cost justification information provided in Allen District’s nonrecurring rate case, Case No. 2013-00188, and has adjusted these charges by removing Field Labor Costs and Office/Clerical Labor Costs.¹³ For nonrecurring charges that occur after normal business hours, following Case No. 2020-00141 and 2020-00167, Staff removed the office/clerical labor costs. Staff also adjusted the mileage rate to the current allowable rate by the Internal Revenue Service (IRS) of \$0.575 per mile.¹⁴ Such adjustments result in the following revised nonrecurring charges:

<u>Nonrecurring Charge</u>	<u>Normal Hours</u>	<u>After Hours</u>
Connection Charge	\$42.50	\$88.50
Meter Reread Charge	\$25.50	
Meter Test Charge	\$39.00	
Returned Check Fee	\$10.25	
Reconnect Fee	\$11.50	\$88.50
Service Investigation Charge	\$25.50	\$71.50

The adjustments to the Nonrecurring Charges results in a decrease to the charges and an increase to the total revenue requirement of \$33,298 as shown below.¹⁵

¹² Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020) and Case No. 2020-00167, *Electronic Application of Ohio County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 3, 2020).

¹³ Case No. 2013-00188, *Tariff Filing of Allen County Water District to Revise Its Non-Recurring Charges*, (Ky. PSC Dec. 17, 2013).

¹⁴ <https://www.irs.gov/tax-professionals/standard-mileage-rates>

¹⁵ Allen District’s Response to Staff’s Second Request for Information, (filed Nov. 16, 2020), Item 3.

Nonrecurring Charges

Charges	Utility Pro Forma	Adjustment	Staff Pro Forma
Service Calls	\$ 2,304	\$ (918)	\$ 1,386
Disconnect/Reconnect Charge	47,872	(31,790)	16,082
Meter Reread Charge	640	(255)	385
Meter Test Charge	200	(78)	122
Returned Check Charge	863	(257)	606
Totals	\$ 51,879	\$ (33,298)	\$ 18,581

(D) Other Water Revenues. In its application, Allen District proposed a decrease to Other Water Revenues of \$49,975¹⁶ to reclassify the other Water Revenues into the correct accounts. First, Allen District proposed to move \$16,845 into Sales for Resale, because it was the sales to the city of Scottsville and are now shown in the Sales for Resale account.¹⁷ Staff agrees that the city of Scottsville sales should be a part of Sales for Resale, and accounted for this in its adjustment A. Next, Allen District sought to reclassify \$33,129 as Line Extension Revenue, which is a capital contribution.¹⁸ Line Extension Revenue is generated when a customer wants an extension to the existing water line. According to Allen District's CPA, the corresponding expenses related to the Line Extensions have already been capitalized, so no further adjustment is required.¹⁹ Staff agrees with Allen District's desire to reclassify these revenues into the correct accounts. Accordingly, Staff decreased Pro Forma Other Water Revenues by a net of \$49,975.

¹⁶ Application, Exhibit 5, Adjustment D.

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ Per phone conversation with Michael Montgomery, CPA, on December 2, 2020.

(E) Salaries and Wages- Employees. Allen District proposed to increase its test-year salaries and wages expense by \$15,884 to reflect a 3 percent raise received by all of their employees on July 1, 2020, as well as \$24,960 to account for the hiring of an additional employee for a total pro forma adjustment of \$40,844.²⁰ In addition in its review, Staff discovered that nine full time employees have left the utility and only four new employees have been hired to replace them. For the five remaining positions, Staff removed the corresponding salaries from Pro Forma operations, as during a conversation with Staff, Allen District indicated that the utility does not plan to replace them. Staff normalized Salaries and Wages Expense using test-year hours worked and current pay rates, which include the test-year pay raise. Accordingly, Staff decreased Pro Forma Salaries and Wages expense by \$68,530.

Job Title	Total Hours	Test Year	Pro Forma Wage Rate	Pro Forma	Test Year	Pro Forma	Pro Forma Overtime Wages	Total Pro Forma Wages
		Normal Hours		Normal Wages	Overtime Hours	Overtime Wage Rate		
Customer Service Specialist/Asst. Mgr.	2,048.50	1,925.75	\$ 15.54	\$ 29,926	122.75	\$ 23.31	\$ 2,861.30	\$ 32,787
Customer Service Specialist	1,865.25	1,792.50	12.00	21,510	72.75	18.00	1,309.50	22,820
Customer Service Specialist	2,033.25	1,919.25	15.09	28,961	114.00	22.64	2,580	31,542
Office Manager	2,008.00	2,008.00	23.21	46,606	-	34.82	-	46,606
Customer Service Specialist	683.25	652.00	12.36	8,059	31.25	18.54	579.38	8,638
General/District Manager	2,044.00	2,008.00	27.84	55,903	36.00	41.76	1,503.36	57,406
Meter Reader - Laborer	2,118.50	1,936.50	21.85	42,313	182.00	32.78	5,965.05	48,278
Meter Reader/Labor Hand	1,213.00	1,129.00	12.36	13,954	84.00	18.54	1,557.36	15,512
Public Relations/Service Tech/Meter Reader	2,201.50	1,936.00	14.56	28,188	265.50	21.84	5,798.52	33,987
Operator/Laborer/Leak Detection	2,280.00	1,955.00	13.89	27,155	325.00	20.84	6,771.38	33,926
Certified Operator/Samples	2,390.50	1,964.00	16.69	32,779	426.50	25.04	10,677.43	43,457
Meter Reader/Labor Hand	2,263.00	1,991.00	11.00	21,901	272.00	16.50	4,488.00	26,389
Meter Reader/Labor Hand	1,708.00	1,549.50	13.86	21,476	158.50	20.79	3,295.22	24,771
Meter Reader/Labor Hand	156.50	136.00	12.36	1,681	20.50	18.54	380.07	2,061
Meter Reader/Labor Hand	1,351.00	1,183.50	13.76	16,285	167.50	20.64	3,457.20	19,742
Custodian	0		Salary	13,000	-			13,000
		24,086.00						
						Total Pro Forma Wages		\$ 460,921
						Test Year Pro Forma Wages		\$ 529,451
						Pro Forma Adjustment		\$ (68,530)

(F) Employee Pensions and Benefits. In its application, Allen District requested an increase to retirement benefits of \$4,741 to account for the increased contribution resulting from the increase in Salaries and Wages requested in its application.²¹ Staff

²⁰ Application, Attachment 5, Adjustment F.

²¹ *Id.*

conferred with Allen District, and the four employees who contributed to the old retirement and pension account are still with the utility and there was no change in the amount contributed to that retirement account. The newer 457(b) retirement account has five employees who contribute to it with a matching of 5 percent of Salaries; therefore, Allen District is correct that as Salaries increase the contribution amount will increase. Staff calculated the continuing contribution amount resulting in an increase to pension and retirement expense of \$221 as shown below.

<u>457(b) Retirement Plan Increase</u>	
2019 Salaries	147,145
plus: 3% salary increase	<u>4,414</u>
Total contributing Salaries	151,559
times: 5% matching	7,578
Test year Contributions	<u>7,357</u>
Retirement adjustment	<u><u>\$ 221</u></u>

(G) Wages and Salaries-1099 Back Pay. During the test year, Allen District reported test-year Salaries for Commissioners of \$39,715.²² However, this amount includes both \$30,000 for Commissioner’s Salaries and \$9,715 for back pay for two employees who received raises in the previous year but inadvertently did not receive the pay increase from the raise. The increased pay rate for the employees is included in the 2019 Employees Salaries and Wages therefore this is not a routine transaction in the normal business and should be removed from the test year. Therefore, Staff reduced Commissioner’s Salaries and Wages by \$9,715.

²² *Id.*, Attachment 5.

(H) Employee Health Insurance. Allen District proposed an adjustment to decrease Employee Pensions and Benefits of \$34,857 since Allen District currently pays 100 percent of the monthly premiums for single health coverage, vision, dental, and life insurance for its eligible full-time employees.²³ Staff notes that the Commission has consistently made ratemaking adjustments to reduce the cost of employee benefit packages paid by some utilities when certain aspects of those benefit packages were found to be unreasonable based on a review of total salaries and fringe benefits. The Commission continues to place greater emphasis on evaluating employees' total compensation packages, including both salary and benefits programs, for market and geographic competitiveness to ensure the development of a fair, just and reasonable rate. It has found that in most cases, 100 percent of employer-funded health care does not meet those criteria.

Consistent with past precedent in which the Commission has reduced benefit expenses for utilities that pay 100 percent of an employee's health insurance coverage; Staff reduced Allen District's single health insurance premiums by 21 percent,²⁴ and single dental insurance premiums by 60 percent the national average employee contribution rate.²⁵ Factoring in for the preceding, Staff decreased employee pensions and benefits by \$32,087, as shown in the calculation below.

²³ *Id.*, Adjustment G.

²⁴ Bureau of Labor Statistics, Healthcare Benefits, March 2017, Table 10, private industry workers. (<https://www.bls.gov/ncs/ebs/benefits/2017/ownership/private/table10a.pdf>)

²⁵ Willis Benefits Benchmarking Survey, 2015 (https://www.willis.com/documents/publications/Services/Employee_Benefits/Willis_Survey_011216_R1.pdf)

Type of Premium	Employer Contributions	Average Employee Contribution Rate	Monthly Premium Adjustment	Pro Forma Monthly Premium
Health Insurance ²⁵	\$ 14,146	21%	\$ (2,971)	\$ 11,175
Life Insurance	64			64
Dental Insurance	289	60%	(174)	115
Vision Insurance	83			83
Total	\$ 14,583			
Total Pro Forma Monthly Premium				11,438
Times: 12 Months				<u>12</u>
Total Annual Pro Forma Premium				137,256
Less: Test Year				<u>(169,343)</u>
Adjustment				<u>\$ (32,087)</u>

(l) Expenses Attributable to Water Loss. In its application, Allen District proposed an adjustment to Purchased Waster and Purchased Power to account for excess water loss²⁷. This adjustment is in accordance with Commission precedence, and Staff agrees with Allen District proposed adjustment and decreased Purchased Water Expense by \$112,842, and Purchased Power Expense by \$10,488. The adjustments result in a net decrease to Revenue Requirement of \$123,330 as shown in the table below.

²⁶ Allen District has 15 full time employees who receive single payer insurance, and one part time employee who does not receive benefits.

Type	Single Payer Monthly contribution
Medical	\$ 943.07
Dental	19.29
Life	Varies based on age
Vision	5.56

²⁷ Application, Exhibit 5, Adjustment H.

	<u>Purchased Water</u>	<u>Purchase Power</u>
Purchased Water from 2019 Annual Report	\$ 709,705	\$ 65,964
Times: Water loss Above 15 Percent	-15.9%	-15.9%
Purchased Water Expense Reduction	(112,842)	<u>(10,488)</u>
		<u><u>\$(123,330)</u></u>

Staff finds that the adjustments to purchased power expense and purchased water expense amounting to \$123,330 should be collected and set aside as a surcharge fund. The use of a surcharge is consistent with prior Commission action in cases involving water districts with excessive unaccounted-for water loss.²⁸ In establishing water-loss surcharges, the Commission recognized that the adjustments required to be made to comply with the 15 percent line-loss limitation in 807 KAR 5:066, Section 6(3), could severely restrict cash flow and could impair a water district's ability to take the necessary action to focus on its leak detection and repair. Using a surcharge to fund a water district's water loss reduction project allows the Commission to place strict controls governing the surcharge proceeds to ensure their effective use, public acceptance of the surcharge, and public confidence in the water district's use of those funds. In its report entitled, *"Confronting the Problems Plaguing Kentucky's Water Utilities: An Investigative Report by the Kentucky Public Service Commission November 2019"* that was fully incorporated

²⁸ See, e.g., 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).

in the final Order in Case No. 2019-00041, Appendix L, the Commission recommended more frequent rate cases and pursuing qualified infrastructure improvement surcharges, the proceeds of which will be devoted exclusively to infrastructure improvement and replacement.²⁹

Allen District should develop and submit a qualified infrastructure improvement plan in furtherance of the recommendations from Case No. 2019-00041 to be approved by the Commission and use the surcharge funds to further reduce its water loss as part of that plan. A monthly surcharge is a reasonable means for Allen District to recover the cost of an infrastructure improvement and water leak detection program in order to reduce the increased expense and lost revenue from unaccounted-for water loss. Allen District should assess a monthly water loss reduction surcharge of \$1.77³⁰ per active meter over 48 months. Allen District should be permitted to assess a surcharge to fund its unaccounted-for water loss reduction efforts to comply with the Commission's final Order in Case No. 2019-00041. Allen District should be restricted to expending any funds collected under the surcharge subject to authorization by the Commission. Allen District should file a qualified infrastructure improvement plan, including a comprehensive unaccounted-for water loss reduction plan that establishes priorities, a time schedule for eliminating each source of unaccounted-for water loss, and provides a detailed spending plan for the proceeds of the requested surcharge.

²⁹ See Case No. 2019-00041, *Electronic Investigation into Excessive Water Loss by Kentucky's Jurisdictional Water Utilities* (Ky. PSC Nov. 22, 2019), Appendix L, *Confronting the Problems Plaguing Kentucky's Water Utilities: An Investigative Report by the Kentucky Public Service Commission November 2019* at 24–25.

³⁰ $\$112,842$ (Purchased Water) + $\$10,488$ (Purchased Power) = $\$123,330$ (Annual Surcharge Collections) \div 5,810 (Number of Active Meters as of December 31, 2019) = $\$21.23$ (Annual Surcharge Collections per Active Meter) \div 12 (Months) = $\$1.77$.

(J) Depreciation Expense. In its application, Allen District reported its Depreciation expense as \$546,044.³¹ To evaluate the reasonableness of the depreciation practices of small water utilities, the Commission has historically relied upon the report published in 1979 by the National Association of Regulatory Utility Commissioners (NARUC) titled Depreciation Practices for Small Water Utilities (NARUC Study). When no evidence exists to support a specific life that is outside the NARUC ranges, the Commission has historically used the midpoint of the NARUC ranges to depreciate the utility plant. Upon examination, Staff found that several items that had already been fully depreciated were included in Allen District's calculation, also while Staff agrees with Allen District's methodology, Staff calculated different amounts when applying the methodology from the NARUC Study. Staff removed these assets and recalculated the totals; Staff's adjustment reduced test-year depreciation by a further \$8,167 as shown in the table below. Therefore, Staff reduced Depreciation expense by a net reduction of \$115,022.

Asset	Original Cost	Current Depreciation	End Depreciation	Book Value	Adjusted Life	Adjusted Depreciation	Difference
303- Land, Land Rights	\$ 314,512	-	\$ 1	\$ 314,511	-	-	-
304- Structures	1,230,921	\$ 24,618	68,313	1,162,608	37.5	\$ 32,825	\$ 8,207
305- Office Building	560,378	18,678	364,246	196,132	37.5	14,943	(3,735)
311- Pumping Equipment	713,281.35	14,266	196,764	516,517.00	25.0	28,531	14,265
330- Distrib Reservoir & Stand	1,384,313.47	30,296	528,624	855,689.56	45.0	30,763	467
331- Transmission Dist Mains	12,913,000.56	258,260	5,411,989	7,501,011.93	62.5	206,608	(51,652)
333- Services	454,990.98	9,100	253,157	201,834.15	40.0	11,375	2,275
334- Meters	1,767,407.51	87,437	796,685.28	970,722.23	40.0	39,901	(47,536)
335- Hydrants	43,859.89	877	20,088.04	23,771.85	50.0	877	-
340- Office Furniture & Equip	221,191.30	11,258	167,827.65	53,363.65	10.0	9,848	(1,410)
341- Transportation Equip	329,374.50	22,334	279,201.80	50,172.70	7.0	16,635	(5,699)
343- Tools, Shop & Garage Equipment	68,426.20	3,981	40,515.00	27,911.00	17.5	2,503	(1,478)
345- Power Operated Equipment	507,219.23	50,722	304,332.00	202,887.71	20.0	25,361	(25,361)
Remainder of Group	123,276.51	12,328	27,785.66	95,490.85	12.5	9,863	(2,465)
345.1-Communications Equipment	55,248.55	1,889	50,602.00	4,646.55	10.0	989	(900)
Total	20,687,401	546,044	8,510,131	12,177,270		431,022	(115,022)

Proforma Depreciation Expense	546,044
Test Year Depreciation Expense	431,022
Pro Forma Adjustment	(115,022)
Proposed Pro Forma Adjustment	(106,855)
Additional Adjustment	(8,167)

³¹ Application, Exhibit 5.

(K) Taxes Other than Income, FICA. Allen District proposed an adjustment to FICA to reflect Pro Forma Salaries and Wages changes.³² However, as discussed in Adjustment (F), Staff decreased Salaries and Wages- Employees by \$68,530. As shown below, Staff determined that test-year FICA taxes should be decreased by \$5,243 to reflect the decrease to Pro Forma Salaries and Wages-Employees expense.

Taxes other than Income (Payroll Tax)	
Salaries and Wages increase	\$ (68,530)
Times: FICA Rate	7.65%
Tax Adjustment	\$ (5,243)

(L) Nonutility Income. During the test year, Allen District proposed an adjustment decreasing Nonutility Income by \$77,816 to account for unrealized gain on temporary investments. Staff Agrees with the adjustment since unrealized gain is not actual income received therefore it should be removed from Allen District's Revenue Requirement.

OVERALL REVENUE REQUIREMENT AND REQUIRED REVENUE INCREASE

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)

³² *Id.*, Adjustment F.

recovery of depreciation expense, a noncash item, to provide working capital;³³ (3) the average annual principal and interest payments on all long-term debts, and (4) working capital that is in addition to depreciation expense.

	Allen County Water District	Staff	
Pro Forma Operating Expenses	\$ 2,326,148	\$ 2,191,094	
Plus: Average Annual Principal and Interest Payments	474,621	474,621	(1)
Additional Working Capital	<u>94,924</u>	<u>94,924</u>	(2)
Overall Revenue Requirement	2,895,694	2,760,639	
Less: Other Operating Revenue	(97,955)	(64,657)	(3)
Interest Income	(75,875)	(75,875)	
Net nonutility Income	<u>(8,907)</u>	<u>(8,907)</u>	
Revenue Required from Rates	2,712,957	2,611,200	
Less: Pro Forma Present Rate Service Revenues	<u>(2,343,426)</u>	<u>(2,343,427)</u>	
Required Revenue Increase	<u>\$ 369,531</u>	<u>\$ 267,773</u>	
Percentage Increase	<u>15.8%</u>	<u>11.4%</u>	

1. Average Annual Principal and Interest Payments. At the time of Staff's review, Allen District had two outstanding United States Department of Agriculture, Rural Development (USDA/RD) Loans, one Kentucky Infrastructure Authority loan, and two Kentucky Rural Water Finance Corporation bonds. In its application Allen District requested recovery of the average annual principal, interest and fee payments on its indebtedness based on a five-year average of the annual principal, and interest and fee

³³ 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).

payments for the years 2021 through 2025.³⁴ Staff agrees with the methodology Allen District proposes. As shown below, Staff calculated an Average Principal and Interest Payment of \$474,621.

Year	Annual Debt Payment													Totals
	RD Loan 91-12		RD Loan 91-14		KRWFC Series 2012 D			KRWFC Series 2013 C			KIA Loan 2020			
	Principal	Interest	PRI	INT	PRI	INT	Fees	PRI	INT	FEES	PRI	INT	FEES	
2021	\$28,500	\$60,266	\$14,000	\$21,465	\$105,000	\$ 81,173	\$ 450	\$25,000	\$ 1,613	\$250	\$100,733	\$48,499	\$4,850	\$ 491,798
2022	30,000	58,950	14,000	21,045	110,000	77,864	450	25,000	538	250	102,758	46,474	4,647	491,975
2023	31,000	57,578	14,500	20,618	110,000	74,289	450				104,823	44,409	4,441	462,107
2024	32,500	56,149	15,000	20,175	115,000	70,519	450				106,930	42,302	4,230	463,255
2025	34,000	54,653	15,500	19,718	120,000	66,404	450				109,079	40,153	4,015	463,971
Total	156,000	287,595	73,000	103,020	560,000	370,248.00	2,250	50,000	2,150	500	524,323	221,837	22,183	\$ 2,373,106
											Divided by: 5 years			5
											Average Principal and Interest			\$ 474,621

2. 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 average annual debt payments. Allen District requested recovery of an allowance for working capital that is equal to 120 percent of its average annual debt payments for its bond payable to the USDA/RD, the Kentucky Infrastructure Authority, and Kentucky Rural Water Finance Corporation at the time of its application.

USDA/RD requires that Allen District charge rates that produce net revenues that are at least 120 percent of its average annual debt payments. Following the Commission’s historic practice, Staff agrees with Allen District’s methodology. Therefore, \$94,924 is included in the revenue requirement.

³⁴ Application, Exhibit 5, Table B.

Average Annual Principal and Interest	\$ 474,621
Times: DSC Coverage Ratio	<u>120%</u>
Total Net Revenues Required	569,545
Less: Average Annual Principal and Interest Payments	<u>(474,621)</u>
Additional Working Capital	<u>\$ 94,924</u>

3. Other Operating Revenue. Other Operating Revenues is the sum of Allen District's revenues not received from water sales. In the application Allen District calculated \$97,955 by combining Forfeited Discounts of \$50,093 and Miscellaneous Service Revenues of \$47,862. Taking Staff's adjustments (B), (C), and (D) into account resulted in a total of \$64,657.³⁵

³⁵ Forfeited Discounts of \$50,093 and Miscellaneous Service Revenues of \$14,564.

Signatures

Prepared by: William Foley
Revenue Requirements Branch
Division of Financial Analysis

Prepared by: Eddie Beavers
Rate Design Branch
Division of Financial Analysis

APPENDIX

APPENDIX TO A STAFF REPORT OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2020-00296 DATED DEC 16 2020

Monthly Water Rates

General Customers

First 2,000 Gallons	\$21.50	Minimum Bill
Next 3,000 Gallons	.00844	Per Gallon
Next 5,000 Gallons	.00715	Per Gallon
Next 60,000 Gallons	.00654	Per Gallon
Over 70,000 Gallons	.00598	Per Gallon

U.S. Corp of Engineers

First 55,000 Gallons	\$406.90	Minimum Bill
Next 15,000 Gallons	.00654	Per Gallon
Over 70,000 Gallons	.00598	Per Gallon

Mobile Home Parks

First 10,000 Gallons	\$75.34	Minimum Bill
Next 60,000 Gallons	.00654	Per Gallon
Over 70,000 Gallons	.00598	Per Gallon

Wholesale Rates

.00369 Per Gallon

Nonrecurring Charges

Meter Reread Charge	25.50
Meter Test Charge	39.00
Connection/Reconnection Charge	42.50
Connection/Reconnection Charge After Hours	88.50

Service Investigation Charge	25.50
Service Investigation Charge After Hours	71.50
Returned Check Charge	10.25
Security Deposit	76.75

*Allen County Water District
330 New Gallatin Road
P. O. Box 58
Scottsville, KY 42164

*DeAnn Marquez
Allen County Water District
330 New Gallatin Road
P. O. Box 58
Scottsville, KY 42164

*Alan Vilines
Kentucky Rural Water Association
Post Office Box 1424
1151 Old Porter Pike
Bowling Green, KENTUCKY 42102-1424