

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

| | |
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| ELECTRONIC APPLICATION OF LAKE VILLAGE) | CASE NO. |
| WATER ASSOCIATION, INC. FOR A RATE) | 2022-00068 |
| ADJUSTMENT PURSUANT TO 807 KAR 5:076) | |

NOTICE OF FILING OF COMMISSION STAFF'S REPORT

Notice is hereby given that, in accordance with the Commission's Order of March 21, 2022, the attached report containing the findings of Commission Staff regarding the Applicant's proposed rate adjustment has been filed in the record of the above-styled proceeding. Pursuant to the Commission's March 21, 2022 Order, Lake Village Water Association, Inc. (Lake Village Water) is required to file written comments regarding the findings of Commission Staff no later than 14 days from the date of this report. The Commission directs Lake Village Water to the Commission's July 22, 2021 Order in Case No. 2020-00085¹ regarding filings with the Commission.



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

DATED AUG 01 2022

cc: Parties of Record

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

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COMMISSION STAFF'S REPORT ON
LAKE VILLAGE WATER ASSOCIATION, INC.

Lake Village Water Association, Inc. (Lake Village Water), a water association organized pursuant to KRS Chapter 273, provides water service to approximately 2,275 residential and commercial customers in Boyle and Mercer counties, Kentucky.¹ In the final Order for Case No. 2020-00021,² Lake Village Water was ordered to file an application by March 9, 2022, for either a traditional adjustment in rates or for an alternative rate adjustment to ensure its revenue is sufficient to support adequate and reliable service.

On March 4, 2022, Lake Village Water tendered its application to the Commission requesting to adjust its water rates pursuant to 807 KAR 5:076, and it was accepted as filed. To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated March 21, 2022.

¹ *Annual Report of Lake Village Water Association to the Public Service Commission for the Calendar Year Ended December 31, 2020* (2020 Annual Report) at 12 and 49.

² See Case No. 2021-00020, *Electronic Application of the Lake Village Water Association, Inc. to Issue Securities in the Approximate Principal Amount of \$2,100,000 for the Purpose of Refunding Certain Outstanding Indebtedness of the Association Pursuant to the Provisions of KRS 278.300 and 807 KAR 5:001* (Ky. PSC March 9, 2021).

Pursuant to 807 KAR 5:066, Section (6)3, water loss is limited to 15.00 percent for ratemaking purposes. The Commission Staff notes that Lake Village Water reported a water loss of 22.55 percent in its 2020 Annual Report.³ At a 22.55 percent water loss, the annual cost of water loss in excess of 15.00 percent is \$42,819 and the total annual cost of water loss to Lake Village Water is \$127,866.⁴

To comply with the requirements of 807 KAR 5:076, Section 9, Lake Village Water based its requested rates on a historic test period that coincides with the reporting period shown in its most recent Annual Report on file with the Commission: the calendar year ended December 31, 2020.⁵

Using the Debt Service Coverage (DSC) method historically used by the Commission, its pro forma test-year operations, and its updated Debt Service payments, Lake Village Water determined in its updated calculations it could justify a revenue increase of \$184,634, or 12.60 percent.⁶ The rates requested by Lake Village Water

³ 2020 Annual Report at 57 and 58.

⁴

| | Purchased Water | Purchased Water | Total |
|--|-----------------|-----------------|--------------|
| Allowable Purchases | \$ 552,238 | \$ 14,885 | \$ 567,123 |
| Multiplied by: Water Rate per 1,000 Gallons | -7.55% | -7.55% | -7.55% |
| Cost of Line loss in Excess of the 15% Limit | \$ (41,695) | \$ (1,125) | \$ (42,819) |
| | Purchased Water | Purchased Water | Total |
| Allowable Purchases | \$ 552,238 | \$ 14,885 | \$ 567,123 |
| Multiplied by: Water Rate per 1,000 Gallons | -22.55% | -22.55% | -22.55% |
| Total Cost of Line Loss | \$ (124,530) | \$ (3,357) | \$ (127,886) |

⁵ Application at 3.

⁶ Application, Attachment 4, Revenue Requirements.

would increase the monthly bill of a typical residential customer using 4,000 gallons per month by \$7.56, from \$47.54 to \$55.10, or approximately 15.90 percent.⁷

| | |
|--|--------------------|
| Pro Forma Operating Expenses | \$ 1,410,078 |
| Plus: Average Annual Debt Service | 241,511 |
| Debt Service Coverage Requirement | <u>48,301</u> |
| Overall Revenue Requirement | 1,699,891 |
| Less: Other Operating Revenue | (48,776) |
| Interest Income | <u>(720)</u> |
| Revenue Required from Water Sales | 1,650,396 |
| Less: Normalized Revenues from Water Sales | <u>(1,465,765)</u> |
| Required Revenue Increase/(Decrease) | <u>\$ 184,631</u> |
| Percentage Increase | <u>12.60%</u> |

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

Commission Staff’s findings are summarized in this report. Mark Frost reviewed Lake Village Water’s Pro Forma Operating Expenses and its Overall Revenue Requirement. Liz Stefanski reviewed Lake Village Water’s reported revenues and rate design.

⁷ Application, Attachment 1, Customer Notice. \$55.10 [\$53.53 (Average Bill Proposed Water Rates) + \$1.57 (Water Loss Reduction Surcharge)] - \$47.54 (Average Bill Current Water Rates) = \$7.56 (Total Difference in Customer Bill) ÷ \$47.54 (Average Bill Current Water Rates) = 15.90%

SUMMARY OF FINDINGS

1. Overall Revenue Requirement and Required Revenue Increase. By applying the DSC method, as generally accepted by the Commission, Commission Staff found that Lake Village Water's required Overall Revenue Requirement is \$1,706,203. To meet the Overall Revenue Requirement, Lake Village Water requires a \$172,178, or 11.71 percent revenue increase to Pro Forma present rate revenues.

2. Monthly Water Service Rates. In the Application, Lake Village Water proposed to increase all of its monthly retail water service rates, evenly across the board by approximately 12.60 percent. Lake Village Water has not performed a cost of service study (COSS). Lake Village Water stated that it did not consider filing a COSS with the current rate application as there were no material changes in its system and that Lake Village Water would consider preparing a new COSS if material changes in customer usage patterns were to occur.⁸ 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, Commission Staff followed the method proposed by Lake Village Water and allocated the \$220,382 revenue increase across the board to Lake Village Water's monthly retail water service rates. The rates set forth in the Appendix to this report are based upon the revenue requirement, as calculated by Commission Staff, and will produce sufficient revenues from water sales to recover the \$1,642,002 Revenue Required from Rates, an

⁸ Lake Village Water's Response to Commission Staff's First Request for Information (Staff's First Request) (filed Mar. 21, 2022), Item 5.

approximate 11.71 percent increase. These rates will increase a typical⁹ residential customer's monthly water bill from \$47.54 to \$53.09,¹⁰ an increase of \$5.55, or approximately 11.67 percent. An additional monthly charge of \$1.61 per customer will be included for the Water Loss Reduction Surcharge.¹¹

3. Nonrecurring Charges. Following the Commission's recent decisions,¹² Commission Staff has reviewed Lake Village Water's Nonrecurring Charges. The Commission found that because association 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. Lake Village Water provided the cost justification information for the nonrecurring charges,¹³ and updated the information with a supplemental filing on June 1, 2022. Commission Staff reviewed the cost justification information provided by Lake Village Water and have adjusted these charges by removing Field Labor Costs and Office/Clerical Labor Costs from those charges that occur during normal business hours. The cost justification information provided for the Returned Check charge indicated that the fee was initiated by Lake

⁹ A typical residential customer uses an average of 4,000 gallons per month.

¹⁰ \$54.61 for water usage plus \$1.61 for Water Loss Surcharge Reduction= \$56.22

¹¹ \$41,695 (Purchased Water) + \$1,125 (Purchased Power) = \$42,819 (Annual Surcharge Collections) ÷ 26,587 (Number of Test-Year Bills) = \$1.61.

¹² Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020); Case No. 2020-00167, *Electronic Application of Ohio County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 3, 2020); Case No. 2020-00196, *Electronic Application of West Daviess County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020); and Case No. 2020-00195, *Electronic Application of Southeast Daviess County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020).

¹³ Lake Village Water's Response to Staff's First Request, Item 9.

Village Water's bank and was not adjusted. Such adjustments result in the following revised Nonrecurring Charges:

| <u>Nonrecurring Charge</u> | <u>Current Charge</u> | <u>Revised Charge</u> |
|-----------------------------|-----------------------|-----------------------|
| Late Payment Charge | 10% | 10% |
| Connection/Turn-on Charge | \$25.00 | \$ 7.00 |
| Customer Request Disconnect | \$25.00 | \$ 7.00 |
| Field Collection Charge | \$25.00 | \$ 7.00 |
| Reconnection Charge | \$45.00 | \$14.00 |
| Meter Test Charge | \$20.00 | \$ 7.00 |
| Returned Check | \$10.00 | \$10.00 |

The adjustments to the Nonrecurring Charges results in an increase to Other Water Revenue of \$931 and a decrease to Retail Sales of Water of \$2,950 as shown below.¹⁴

| | Number of Occurrences | Current Charge | Revised Charge | Pro Forma | Other Water Revenue |
|-----------------------------|-----------------------|----------------|----------------|-----------|---------------------|
| Late Payment Penalty | | | | | |
| Connection Turn-On Charge | 61 | 25 | 7 | 427 | 1,525 |
| Customer Request Disconnect | 47 | 25 | 7 | 329 | 1,175 |
| Field Collection Charges | 0 | 25 | 7 | - | - |
| Reconnection Fee | 2 | 45 | 14 | 28 | 90 |
| Meter Test Request | 1 | 20 | 7 | 7 | 20 |
| Returned Check Charge | 14 | 10 | 10 | 140 | 140 |
| | | | | \$ 931 | \$ 2,950 |

4. Request for Surcharge. Lake Village Water requested the Commission authorize a water loss reduction surcharge of \$1.57 per customer per month to assist in lowering system water loss to more acceptable levels.¹⁵ Lake Village Water explained in its customer notice that it was requesting the surcharge not to exceed a time period of 48 months.¹⁶ Lake Village Water's requested surcharge of \$1.57 per customer was

¹⁴ Lake Village Water's Response to Staff's First Request, Item 9, and updated filing of June 1, 2022.

¹⁵ Application, Attachment 2, Reasons for Application.

¹⁶ Application, Attachment 1, Customer Notice.

calculated by dividing the \$41,691 proposed adjustment to Purchased Water expense by the number of test-year bills of 26,587.¹⁷ No formal plan or explanation was given by Lake Village Water that indicated any specific future use of the surcharge funds. Commission Staff recalculated the monthly water loss surcharge to be \$1.61¹⁸ per active meter using the water loss adjustment described in Adjustment (I) below.

The use of a surcharge is consistent with prior Commission action in cases involving water utilities with excessive unaccounted-for water loss in excess of 30 percent.¹⁹ Further, the Commission has ordered surcharges even when a utility has not specifically requested a surcharge,²⁰ and recently, the Commission has allowed water utilities with reported water loss above 15 percent threshold to assess water loss reduction surcharges.²¹ Recognizing prior Commission precedent to allow the use of surcharges to assist utilities in obtaining the proper funding needed to combat water loss, Commission Staff recommends the Commission approve Lake Village Water's request and authorize the surcharge for a temporary period of 48 months, with a review of the

¹⁷ Lake Village Water's Response to Staff's First Request, Item 3, Excel Workbook: 3_Rate_Study.xlsx; Tab: Water Loss.

¹⁸ \$41,695 (Purchased Water) + \$1,125 (Purchased Power) = \$42,819 (Annual Surcharge Collections) ÷ 26,587 (Number of Test-Year Bills) = \$1.61.

¹⁹ See Case No. 96-126, *An Investigation into the Operations and Management of Mountain Water District* (Ky. PSC Aug. 11, 1997); Case No. 2011-00217, *Application of Cannonsburg Water District for (1) Approval of Emergency Rate Relief and (2) Approval of the Increase in Nonrecurring Charges*, (Ky. PSC June 4, 2012); Case No. 2018-00017, *Application of Martin County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 5, 2018); Case No. 2018-00429, *Application of Graves County Water District for an Alternative Rate Adjustment* (Ky. PSC Sept. 30, 2019); and Case No. 2019-00119, *Electronic Application of Estill County Water District No. 1 for a Surcharge to Finance Water Loss Control Efforts* (Ky. PSC Mar. 24, 2010); Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020), Order at 11-13.

²⁰ Case No. 2020-00311, *Electronic Application of Cawood Water District for an Alternative Rate Adjustment* (Ky. PSC Apr. 8, 2021), Order at 3.

²¹ See Case No. 2021-00094, *Electronic Application of Garrison-Quincy-Ky-O-Heights Water District for a Rate Adjustment Pursuant to 807 KAR 5:076* (Ky. PSC Nov. 24, 2021).

necessity to continue the surcharge before the temporary period expires. Commission Staff also recommends the Commission establish a separate proceeding to monitor the surcharge and place strict controls over the use of the funds that will be collected from the surcharge. Further Commission Staff recommends the Commission require Lake Village Water to develop a long-term plan to address its aging infrastructure and combat water loss within six months of the final order in this proceeding.

PRO FORMA OPERATING STATEMENT

Lake Village Water's Pro Forma Operating Statement for the test period ended December 31, 2020, as determined by Staff, appears below.

| | Test Year Operations | Pro Forma Adjustments | Adj. Ref. | Pro Forma Operations |
|--|-------------------------|--------------------------|--------------|-------------------------|
| Operating Revenues: | | | | |
| Total Metered Sales | \$ 1,444,027 | \$ 25,798 | A | \$ 1,469,825 |
| Other Water Revenues: | | | | |
| Misc. Service Revenues | 43,776 | (2,019) | B | |
| | | 16,724 | C | |
| | | 5,000 | D | 63,481 |
| Total Operating Revenues | <u>1,487,803</u> | <u>45,503</u> | | <u>1,533,306</u> |
| Operating Expenses: | | | | |
| Operation and Maintenance: | | | | |
| Salaries and Wages - Employees | 363,454 | 24,873 | E | |
| | | (3,240) | F | 385,087 |
| Salaries and Wages - Officers | 23,850 | | | 23,850 |
| Employee Pensions and Benefits | 74,829 | 938 | G | |
| | | (8,507) | H | 67,260 |
| Purchased Water | 552,238 | (41,695) | I | 510,543 |
| Materials and Supplies | 70,450 | (7,560) | F | 62,890 |
| Contractual Services | 14,961 | | | 14,961 |
| Transportation | 11,619 | | | 11,619 |
| Insurance - Gen. Liab. & Workers Comp. | 19,172 | | | 19,172 |
| Insurance Other | 16,164 | | | 16,164 |
| Bad Debt | 4,577 | | | 4,577 |
| Miscellaneous Expenses | 76,063 | (1,125) | I | 74,938 |
| Total Operation and Mnt. Expenses | 1,227,377 | (36,316) | | 1,191,061 |
| Depreciation Expense | 311,352 | (120,388) | J | 190,964 |
| Taxes Other Than Income | 29,963 | 4,399 | K | 34,362 |
| Total Operating Expenses | <u>1,568,692</u> | <u>(152,305)</u> | | <u>1,416,387</u> |
| Net Utility Operating Income | <u>\$ (80,889)</u> | <u>\$ 197,808</u> | | <u>\$ 116,919</u> |

(A) Billing Analysis. In its application, Lake Village Water made an adjustment of \$21,738 to increase Metered Water Sales and provided a billing analysis listing the water usage and water sales revenue for the 12-month test year in its application, with total metered water sales revenue reported as \$1,465,765.²² According to Lake Village Water’s 2020 Annual Report, the total metered water sales revenue reported for the test year was \$1,444,027.²³ Lake Village Water provided usage data,²⁴ and billing adjustment information²⁵ to which Commission Staff calculated a normalized revenue amount based on the statistics compiled in the table below, which include net billing adjustments²⁶ for a normalized revenue of \$1,469,825. Accordingly, Staff increased test year water sales by \$25,798.

| Meter Size | Bills | Gallons Sold | Revenue |
|-------------------------|--------------|---------------------|--------------------|
| 5/8 inch | 26575 | 94,030,200 | 1,256,570.21 |
| Wholesale | 12 | 58,874,000 | 239,028.44 |
| Totals | 26,587 | 152,904,200 | \$1,495,599 |
| Net Billing Adjustments | | | (25,774) |
| | | | <u>\$1,469,825</u> |

(B) Miscellaneous Service Revenues. Lake Village Water provided information about the nonrecurring charges revenue,²⁷ and Staff calculated an adjustment to Other Water Revenue, removing labor costs as discussed above. The adjustments to

²² Application, Attachment 5, Schedule of Adjusted Operations.

²³ 2020 Annual Report at 49.

²⁴ Lake Village Water’s Response to Staff’s First Request, Item 9a-9d.

²⁵ Lake Village Water’s Response to Staff’s First Request, Item 13.

²⁶ Lake Village Water’s Response to Staff’s First Request, Item 13.

²⁷ Lake Village Water’s Response to Staff’s First Request, Item 8.

Nonrecurring Charges results in a decrease to Miscellaneous Service Revenues of \$2,019 as shown below.

| | Other Water Revenue | Pro Forma Adjustment | Pro Forma |
|-----------------------------|---------------------------|-------------------------|---------------|
| Connection Turn-On Charge | 1,525 | (1,098) | 427 |
| Customer Request Disconnect | 1,175 | (846) | 329 |
| Field Collection Charges | - | - | - |
| Reconnection Fee | 90 | (62) | 28 |
| Meter Test Request | 20 | (13) | 7 |
| Returned Check Charge | 140 | - | 140 |
| | <u>\$ 2,950</u> | <u>\$ (2,019)</u> | <u>\$ 931</u> |

(C) Forfeited Discounts. During the test year, Lake Village Water recorded \$3,116 in Forfeited Discounts. Given that the test year occurred during the moratorium regarding the collection of late payment fees due to the COVID-19 pandemic, Commission Staff normalized the revenue from Forfeited Discounts using a three-year average of the reported income from late fees in the years 2017, 2018, and 2019.²⁸ Based upon a three-year average of \$19,840, Commission Staff increased Miscellaneous Service Revenues by \$16,724.

| | |
|----------------------|------------------|
| 2017 | 18,478 |
| 2018 | 21,307 |
| 2019 | <u>19,736</u> |
| 3-Year Average | \$ 19,840 |
| Less: Test Year Fees | <u>(3,116)</u> |
| Pro Forma Adjustment | <u>\$ 16,724</u> |

(D) Management Fee. Lake Village Water provides management services to Mercer County Sanitation District and on July 1, 2021 the annual management fee

²⁸ Lake Village Water's Responses to Commission Staff Third Request for Information (filed June 1, 2022), Item1.

increased from \$35,000 to \$40,000.²⁹ Lake Village Water proposed to increase Miscellaneous Service Revenues by \$5,000 to reflect the management fee increase.³⁰ Lake Village Water's adjustment to reflect the 2021 management fee meets the ratemaking criteria of being known and measurable.³¹ Accordingly, Miscellaneous Service Revenues has been increased by \$5,000.

(E) Salaries and Wages - Employees. Lake Village proposed to increase its test-year Employee Salaries and Wages expense of \$363,454 by \$16,554 for a pro forma Employee Salaries and Wages expense of \$380,008.³² According to Lake Village Water, since the 2020 test period there have been increases in its employee wage rates and changes in personnel.³³ These changes result in Lake Village Water's proposed increase to Employee Salaries and Wages expense of \$16,554.³⁴

²⁹ Application, Attachment 4, Schedule of Adjusted Operations, Reference B and References, Reference B.

³⁰ Application, Attachment 4, Schedule of Adjusted Operations, Reference B and References, Reference B.

³¹ See 807 KAR 5:001, Section 16.1.(a); Case No. 2001-00211, *The Application of Hardin County Water District No. 1 for (1) Issuance of Certificate of Public Convenience and Necessity; (2) Authorization to Borrow Funds and to Issue Its Evidence of Indebtedness Therefor; (3) Authority to Adjust Rates; and (4) Approval to Revise and Adjust Tariff* (Ky. PSC Mar. 1, 2002); Case No. 2002-00105, *Application of Northern Kentucky Water District for (A) an Adjustment of Rates; (B) a Certificate of Public Convenience and Necessity for Improvements to Water Facilities if Necessary; and (C) Issuance of Bonds* (Ky. PSC June 25, 2003); Case No. 2017-00417, *Electronic Proposed Adjustment of the Wholesale Water Service Rates of Lebanon Water Works* (Ky. PSC July 12, 2018); and Case No. 2019-00080, *Electronic Proposed Adjustment of the Wholesale Water Service Rates of the City of Pikeville to Mountain Water District* (Ky. PSC Dec. 19, 2019).

³² Application, Attachment 4, Schedule of Adjusted Operations, Reference C and References, Reference C.

³³ Application, Attachment 4, Schedule of Adjusted Operations, Reference C and References, Reference C.

³⁴ Application, Attachment 4, Schedule of Adjusted Operations, Reference C and References, Reference C.

An adjustment to reflect the actual 2021 wage rates would meet the ratemaking criteria of being known and measurable. Using Lake Village Water’s current staff level of 7 full-time employees, and the 2021 employee wage rates, Commission Staff calculated a pro forma Employee Salaries and Wages expense of \$388,327, which is \$24,873, greater than the reported expense level. Staff’s calculation is in the table below.

| Position Title | Status | Pro Forma | | Pro Forma Wage Rate | Pro Forma | | Total |
|---|--------|-----------|-------------|------------------------|-------------------|-----------------|-------------------|
| | | Reg. Hrs | O. T. Hours | | Reg. Wages | O. T. Wages | |
| Executive Director | Salary | 2,080 | | 1,908.88 | 99,262 | 0 | 99,262 |
| Office Manager | Salary | 1,820 | | 1,139.97 | 59,278 | 0 | 59,278 |
| Maintenance Supervisor | Hourly | 2,080 | 9 | 33.23 | 69,118 | 449 | 69,567 |
| Distribution/Collection Operator | Hourly | 2,080 | 218 | 26.38 | 54,870 | 8,630 | 63,500 |
| Office Clerk | Hourly | 2,080 | | 16.00 | 33,280 | 0 | 33,280 |
| Operator-in-Training | Hourly | 2,080 | | 16.50 | 34,320 | 0 | 34,320 |
| Operator-in-Training | Hourly | 2,080 | | 14.00 | 29,120 | 0 | 29,120 |
| | | | | | <u>\$ 379,248</u> | <u>\$ 9,079</u> | <u>\$ 388,327</u> |
| Pro Forma Employee Salaries & Wages | | | | | | | 388,327 |
| Less: Test-Year Employee Salaries & Wages | | | | | | | <u>(363,454)</u> |
| Pro Forma Adjustment | | | | | | | <u>\$ 24,873</u> |

(F) Tap-on Fees. During the test year, Lake Village Water collected tap-on fees of \$10,800 and correctly recorded the tap-on fees in Account No. 432, Proceeds from Capital Contributions.³⁵ Lake Village Water explained that it recorded the labor and material cost of the meter installations as an operating expense at the time the meters were installed.³⁶ Substituting the tap-on fees for the actual costs it incurred to install the meters, Lake Village Water proposed to deduct 30 percent of the collected tap-on fees or \$3,240 from Salaries and Wages expense and the remaining 70 percent or \$7,560 from the Materials and Supplies expense.³⁷ Commission Staff agrees that Lake Village

³⁵ Application, Attachment 4, Schedule of Adjusted Operations, Reference F and References, Reference F.

³⁶ Application, Attachment 4, Schedule of Adjusted Operations, Reference F and References, Reference F.

³⁷ Application, Attachment 4, Schedule of Adjusted Operations, Reference F and References, Reference F.

Water's adjustments meet the ratemaking criteria of being known and measurable, and Commission Staff included Lake Village Water's proposed adjustments.

(G) Employee 401(k) Pension. Lake Village Water proposed to increase its test-year Employee Pensions and Benefit expense of \$74,829 by \$355 to reflect a slight increase to the employer's contribution to the employee 401(k) Pension expense.³⁸ Applying the 10 percent employer 401(k) contribution rate³⁹ to pro forma Employee Salary and Wages expense of \$388,327 results in Commission Staff's increase to Employee Pensions and Benefit expense of \$938.⁴⁰

(H) Employee Benefits. Lake Village Water proposed to decrease its test year test-year Employee Pensions and Benefit expense of \$74,829 by \$2,105.⁴¹ Lake Village Water currently pays 100 percent of the monthly premiums for health coverage, vision, dental, and life insurance for its eligible full-time employees.⁴² Lake Village Water explained that the Commission currently places the following employer contribution limitations on employee insurance benefits: a 79 percent limit single employee health insurance coverage, a 66 percent on family coverage, and a 60 percent limitation dental

³⁸ Application, Attachment 4, Schedule of Adjusted Operations, Reference E and References, Reference E.

³⁹ Lake Village Water's Responses to Commission Staff's Second Information Request filed May 4, 2022, (Staff's Second Request), Item 1.

⁴⁰ \$388,327 (Pro Forma Employee Salary and Wages expense) x 10% (401(k) Employer Contribution Rate) = \$38,833 (Pro Forma 401(k) Employer Contribution) - \$37,895 (Test-Year Employer 401(k) Contribution) = \$938.

⁴¹ Application, Attachment 4, Schedule of Adjusted Operations, Reference H and References, Reference H.

⁴² Application, Attachment 4, Schedule of Adjusted Operations, Reference H and References, Reference H.

coverage.⁴³ Applying those percentages to the employee insurance premiums is the basis of Lake Village Water's proposed adjustment.⁴⁴ Lake Village Water also proposed an additional adjustment of \$2,274 to reflect a decrease in the employee dental and medical insurance premiums for a total employee benefit adjustment of \$4,829.⁴⁵

Commission 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.

In 2021, the monthly Anthem employee health insurance premium of \$455 included vision and dental coverage. Consistent with past precedent⁴⁶ in which the

⁴³ Application, Attachment 4, Schedule of Adjusted Operations, Reference H and References, Reference H.

⁴⁴ Application, Attachment 4, Schedule of Adjusted Operations, Reference H and References, Reference H.

⁴⁵ Application, Attachment 4, Schedule of Adjusted Operations, Reference G and References, Reference G. $\$2,105$ (Limitation on Employer Contribution) + $\$2,724$ (Premium Decrease) = $\$4,829$ (Total Decrease Employee Benefits).

⁴⁶ 807 KAR 5:001, Section 16(1)(a); Case No. 2001-00211, The Application of Hardin County Water District No. 1 for (1) Issuance of Certificate of Public Convenience and Necessity; (2) Authorization to Borrow Funds and to Issue its Evidence of Indebtedness therefor; (3) Authority to Adjust Rates; and (4) Approval to Revise and Adjust Tariff (Ky. PSC Mar. 1, 2002); Case No. 2002-00105, Application of Northern Kentucky Water District for (A) an Adjustment of Rates; (B) a Certificate of Public Convenience and Necessity for Improvements to Water Facilities if Necessary; and (C) Issuance of Bonds (Ky. PSC June 25, 2003); Case No. 2017-00417, Electronic Proposed Adjustment of the Wholesale Water Service Rates of Lebanon Water Works (Ky. PSC July 12, 2018); and Case No. 2019-00080, Electronic Proposed Adjustment of the Wholesale Water Service Rates of the City of Pikeville to Mountain Water District (Ky. PSC Dec. 19, 2019).

Commission has reduced benefit expenses for utilities that pay 100 percent of an employee’s health insurance coverage, Commission Staff reduced Lake Village Water’s single health insurance premiums by 22 percent. Factoring in the preceding, Commission Staff decreased employee pensions and benefits by \$8,507, as shown in the calculation below.

| | 2022 Monthly Premium | District Contirb % | Annual Premium | Allowable Employer Share | Allowable Employer Premium |
|----------------------------|----------------------------|-----------------------|-------------------|--------------------------------|----------------------------------|
| Medical | \$ 1,820 | 100% | \$ 21,844 | 79% | \$ 17,257 |
| Vision | 0 | 100% | 0 | 100% | 0 |
| Dental | 0 | 100% | 0 | 60% | 0 |
| Life | 72 | 100% | 864 | 100% | 864 |
| TOTAL | \$ 1,892 | | \$ 22,708 | | \$ 18,121 |
| Allowable Employer Premium | | | | | \$ 18,121 |
| Less Annual Premium | | | | | (26,628) |
| Medical Adjustment | | | | | <u>\$ (8,507)</u> |

(l) Excess Water Loss. Commission regulation 807 KAR 5:066, Section 6(3), limits water loss to 15.00 percent for ratemaking purposes unless the Commission finds an alternative level reasonable. Lake Village Water reported a test-year water loss of 22.55 percent, or 7.55 percent above the 15.00 percent allowable limit. To eliminate the cost to purchase, produce, and pump water over the 15.00 percent allowable limit, Lake Village Water proposed to decrease Purchased Water expense by \$41,691.⁴⁷ Commission Staff agrees that Lake Village Water’s proposal to eliminate the costs associated with excessive water loss conforms to the Commission’s current practice.

⁴⁷ Application, Attachment 4, Schedule of Adjusted Operations, Reference I and References, Reference I.

However, as shown in the table below, Commission Staff’s calculations result in decreases to Purchased Water expense and Purchased Power expense of \$41,695, and \$1,125,⁴⁸ respectively.

| | Purchased Water | Purchased Water | Total |
|--|--------------------|-------------------|--------------------|
| Allowable Purchases | \$ 552,238 | \$ 14,885 | \$ 567,123 |
| Multiplied by: Water Rate per 1,000 Gallons | -7.55% | -7.55% | -7.55% |
| Cost of Line loss in Excess of the 15% Limit | <u>\$ (41,695)</u> | <u>\$ (1,125)</u> | <u>\$ (42,820)</u> |

(J) Depreciation. Lake Village Water proposed to decrease its test-year Depreciation expense of \$311,352 by \$120,388 for a pro forma Depreciation expense of \$190,964.⁴⁹ Lake Village Water explained that the Commission typically requires a water utility to adjust its depreciation expense when its depreciation lives fall outside of the ranges recommended in the report published in 1979 by the National Association of Regulatory Utility Commissioners (NARUC) titled *Depreciation Practices for Small Water Utilities* (NARUC Study).⁵⁰ According to Lake Village Water, its adjustment brings the depreciable lives of its assets to or near the midpoint of NARUC’s recommended ranges.⁵¹

To evaluate the reasonableness of the depreciation practices of small water utilities, the Commission has historically relied upon the NARUC Study. When no evidence exists to support a specific life that is inside or outside the NARUC Study ranges,

⁴⁸ Lake Village Water recorded the cost of electricity in its Miscellaneous expense account. Commission Staff’s purchased power adjustment has been made to that expense account.

⁴⁹ Application, Attachment 4, Schedule of Adjusted Operations, Reference J and References, Reference J.

⁵⁰ Application, Attachment 4, Schedule of Adjusted Operations, Reference J and References, Reference J.

⁵¹ Application, Attachment 4, Schedule of Adjusted Operations, Reference J and References, Reference J.

the Commission has historically used the midpoint of the NARUC Study ranges to depreciate a utility plant.

Upon its review of Lake Village Water's depreciation schedule, Commission Staff determined that Lake Village Water's adjusted depreciation lives are at the midpoint of the NARUC Study range for each asset category. Commission Staff agrees that Lake Village Water's proposed depreciation adjustment is reasonable and decreased Depreciation expense by \$120,388.

(K) Payroll Taxes. Lake Village Water proposed to increase its test year Federal Insurance Contributions Act (FICA) Tax expense of \$26,855 by \$2,185 to a pro forma level of \$32,148 to reflect its pro forma Salaries and Wages changes.⁵² Using the pro forma Salaries and Wages expense subject to FICA Taxes of \$408,937 and the current FICA tax rate of 7.65 percent, Commission Staff calculated a pro forma FICA expense of \$31,284, for an increase to Lake Village Water's Payroll Tax expense by \$4,399.⁵³

OVERALL REVENUE REQUIREMENT AND REQUIRED REVENUE INCREASE

Historically, the Commission has applied a DSC method to calculate the revenue requirement of water districts and water associations.⁵⁴ This method allows for recovery of (1) cash-related pro forma operating expenses; (2) depreciation expense, a noncash

⁵² Application, Attachment 4, Schedule of Adjusted Operations, Reference D and References, Reference D.

⁵³ \$408,937 (Salaries and Wages – Employees and Commissioners) x 7.65% (FICA Rate) = \$31,284 (Pro Forma FICA) - \$26,885 (Test-Year FICA expense) = \$4,399.

⁵⁴ See Case No. 2019-00424, *Electronic Application of Grant County Sanitary Sewer District for an Alternate Rate Adjustment* (Ky. PSC May 6, 2020); see also Case No. 2019-00268, *Application of Knott County Water and Sewer District for an Alternative Rate Adjustment* (Ky. PSC Jan. 31, 2020).

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

A comparison of Lake Village Water's and Commission Staff's calculations of the revenue requirement and required revenue increase using the DSC method is shown below:

| | Lake Village Water | Commission Staff |
|--|-----------------------|--------------------|
| Pro Forma Operating Expenses | \$ 1,410,078 | \$ 1,416,387 |
| Plus: Average Annual Debt Service | 241,513 | 241,513 |
| Debt Service Coverage Requirement | <u>48,303</u> | <u>48,303</u> |
| Overall Revenue Requirement | 1,699,894 | 1,706,203 |
| Less: Other Operating Revenue | (48,776) | (63,481) |
| Interest Income | <u>(720)</u> | <u>(720)</u> |
| Revenue Required from Water Sales | 1,650,398 | 1,642,002 |
| Less: Normalized Revenues from Water Sales | <u>(1,465,765)</u> | <u>(1,469,825)</u> |
| Required Revenue Increase/(Decrease) | <u>\$ 184,633</u> | <u>\$ 172,178</u> |
| Percentage Increase | <u>12.60%</u> | <u>11.71%</u> |

Average Annual Principal and Interest Payments.

At the time of Commission Staff's review, Lake Village Water had three outstanding debt issuances.⁵⁵ In calculating its revenue requirement, Lake Village Water used an average annual debt service of \$241,513 and a 0.2 allowance for additional working capital of \$48,333.⁵⁶ Upon its review of Lake Village Water's debt amortization schedules, Commission Staff verified that Lake Village Water's calculations are correct and included them in the calculation of the revenue requirement.

⁵⁵ See 2015 Loan - Case No. 2014-00445, *Application of the Lake Village Water Association, Inc. to Issue Securities in the Approximate Principal Amount of \$1,515,000 for the Purpose of Refunding Certain Outstanding Indebtedness of the Association Pursuant to the Provisions of KRS 278.300 and 807 KAR 5:001* (Ky. PSC Jan. 13, 2015); 2017 Loan, Case No. 2016-00153, *Application of Lake Village Water Association, Inc. for a Certificate of Public Convenience and Necessity to Construct and Finance a Project, Funded by USDA Rural Development Pursuant to the Provisions of KRS 278.023 and KRS 278.020*, (Ky. PSC May 20, 2016); and Loan 2021, Case No. 2021-00020, *Electronic Application of the Lake Village Water Association, Inc. to Issue Securities in the Approximate Principal Amount of \$2,100,000 for the Purpose of Refunding Certain Outstanding Indebtedness of the Association Pursuant to the Provisions of KRS 278.300 and 807 KAR 5:001* (Ky. PSC March 9, 2021).

⁵⁶ Application, Attachment 4, Revenue Requirements.

Signatures

/s/ Mark Frost

Prepared by: Mark Frost
Revenue Requirement Branch
Division of Financial Analysis

/s/ Liz Stefanski

Prepared by: Liz Stefanski
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APPENDIX

APPENDIX TO COMMISSION STAFF'S REPORT OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2022-00068 DATED AUG 01 2022

The following rates and charges are prescribed for the customers in the area served by Lake Village Water Association, Inc. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under the 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 | \$ 29.85 Minimum Bill |
| Next 18,000 Gallons | 0.01162 Per Gallon |
| Over 20,000 Gallons | 0.00938 Per Gallon |

Wholesale Rates

| | |
|-----------------------------|--------------------|
| North Point Training Center | 0.00450 Per Gallon |
|-----------------------------|--------------------|

Water Loss Reduction Surcharge

| | |
|---------------------|-------------------|
| 48 month limitation | \$ 1.61 per month |
|---------------------|-------------------|

Special Nonrecurring Charges

| | |
|-----------------------------|---------|
| Connection/Turn-on Charge | \$ 7.00 |
| Customer Request Disconnect | \$ 7.00 |
| Field Collection Charge | \$ 7.00 |
| Reconnection Charge | \$14.00 |
| Meter Test Charge | \$ 7.00 |
| Return Check Charge | \$10.00 |
| Late Payment Penalty | 10% |

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