

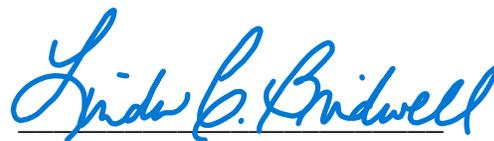
COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

|                                      |   |            |
|--------------------------------------|---|------------|
| ELECTRONIC APPLICATION OF NORTHEAST  | ) |            |
| WOODFORD COUNTY WATER DISTRICT FOR A | ) | CASE NO.   |
| RATE ADJUSTMENT PURSUANT TO 807 KAR  | ) | 2022-00221 |
| 5:076                                | ) |            |

NOTICE OF FILING OF COMMISSION STAFF'S REPORT

Notice is hereby given that, in accordance with the Commission's Order of August 5, 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 August 5, 2022 Order, Northeast Woodford County Water District (Northeast Woodford District) 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 Northeast Woodford District to the Commission's July 22, 2021 Order in Case No. 2020-00085<sup>1</sup> regarding filings with the Commission.



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

DATED NOV 21 2022

cc: Parties of Record

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<sup>1</sup> 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  
NORTHEAST WOODFORD COUNTY WATER DISTRICT

Northeast Woodford County Water District (Northeast Woodford 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 1,014 residential customers and one commercial customer in Woodford County, Kentucky.<sup>1</sup> On July 22, 2022, Northeast Woodford District filed an application with the Commission requesting to adjust its water rates pursuant to 807 KAR 5:076. Northeast Woodford District's last base rate increase was approved in Case No. 2008-00061.<sup>2</sup> To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated August 5, 2022. Northeast Woodford District responded to two requests for information from Commission Staff.

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<sup>1</sup> *Annual Report of Northeast Woodford Water District to the Public Service Commission for the Calendar Year Ended December 31, 2021* (2021 Annual Report) at 12 and 49.

<sup>2</sup> Case No. 2008-00061, *An Application of Rates for Water Service of Northeast Woodford Water District* (Ky. PSC Apr. 30, 2008).

## WATER LOSS

The Commission notes that in its 2021 Annual Report, Northeast Woodford District reported a water loss of 7.87 percent.<sup>3</sup> Commission regulation 807 KAR 5:066(6)(3) states that for ratemaking 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. At a 7.87 percent water loss, the annual cost to Northeast Woodford District is \$33,875.<sup>4</sup>

## DISCUSSION

To comply with the requirements of 807 KAR 5:076, Section 9,<sup>5</sup> Northeast Woodford District used the calendar year ended December 31, 2021, as the basis for its application. In its application Northeast Woodford District determined that a revenue increase of \$103,914, or 16.21 percent over test-year normalized revenues of \$641,090, was warranted.<sup>6</sup> However, during Commissions Staff's analysis, it was discovered

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<sup>3</sup> 2021 Annual Report at 57.

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|                                 | <u>Purchased<br/>Water</u> | <u>Purchased<br/>Power</u> | <u>Total</u>         |
|---------------------------------|----------------------------|----------------------------|----------------------|
| Pro Forma Expenses              | \$ 419,713                 | \$ 10,572                  | \$ 430,285           |
| Multiplied by: Total Water loss | 7.87%                      | 7.87%                      | 7.87%                |
| <br>Total Water Loss            | <br><u>\$ 33,043</u>       | <br><u>\$ 832</u>          | <br><u>\$ 33,875</u> |

<sup>5</sup> The reasonableness of the proposed rates shall be determined using a 12-month historical test period, adjusted for known and measurable changes, which coincides with the reporting period of the applicant's annual report for the immediate past year.

<sup>6</sup> Application, Attachment 4, Revenue Requirements Using Operating Ratio Method.

several expenses in the application were incorrect.<sup>7</sup> Therefore, Northeast Woodford District, using its pro forma test-year operations, recalculated that a revenue increase of \$112,204, or 17.50 percent over test-year normalized revenues of \$641,090, was warranted,<sup>8</sup> as shown in the table below. The updated rates requested by Northeast Woodford District would increase the residential monthly bill of a typical residential customer using 4,000 gallons per month by \$3.82 from \$21.86 to \$25.68, or approximately 17.47 percent.<sup>9</sup>

|   | Northeast Woodford<br>Water District |
|---|--------------------------------------|
| Pro Forma Operating Expenses              | \$ 658,709                           |
| Divided by: Operating Ratio               | 88%                                  |
| Subtotal                                  | 748,533                              |
| Plus: Interest Expense                    | 20,339                               |
| Total Revenue Requirement                 | 768,872                              |
| Less: Other Operating Revenue             | (13,375)                             |
| Interest Income                           | (2,204)                              |
| Revenue Required From Water Sales         | 753,293                              |
| Less: Revenue from Sales at Present Rates | (641,090)                            |
| Required Revenue Increase                 | \$ 112,204                           |
| Percentage Increase                       | 17.50%                               |

<sup>7</sup> Northeast Woodford District's Response to Commission Staff's First Request for Information (Staff's First Request) (filed Sept. 8, 2022), Items 11, 12a, 12b, and 14.

<sup>8</sup> Northeast Woodford District's Response to Staff's First Request, Item 1f\_Rate\_Study\_2021.xlsx, Revenue Requirement Tab.

<sup>9</sup> Northeast Woodford District's Response to Staff's First Request, Item 1f\_Rate\_Study\_2021.xlsx, Tab Bills ORM.

To determine the reasonableness of the rates requested by Northeast Woodford District, Commission Staff performed a limited financial review of Northeast Woodford District'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<sup>10</sup> 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.

Commission Staff's findings are summarized in this report. William Foley reviewed the calculation of Northeast Woodford District's Overall Revenue Requirement. Elizabeth Stefanski reviewed Northeast Woodford District's reported revenues and rate design.

#### SUMMARY OF FINDINGS

1. Overall Revenue Requirement and Required Revenue Increase. By applying the Operating Ratio method, as generally accepted by the Commission, Commission Staff found that Northeast Woodford District's required revenue from water sales is \$726,890 to meet the Overall Revenue Requirement of \$745,885 and that a \$85,800 revenue increase, or 13.38 percent, to pro forma present rate revenues is necessary to generate the Overall Revenue Requirement.

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<sup>10</sup> Commission regulation 807 KAR 5:076, Section 9, sets the standard for the determination of the reasonableness of proposed rates and states, in pertinent part, that the test period shall be "adjusted for known and measurable changes." See also Case No. 2001-00211, *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 Therefore; (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).

2. Monthly Water Service Rates. Northeast Woodford District proposed to increase all of its monthly retail water service rates, evenly across the board by approximately 17.50 percent.<sup>11</sup> Northeast Woodford District has not performed a cost of service study (COSS). Northeast Woodford District 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 Northeast Woodford District would consider preparing a new COSS if material changes in customer usage patterns were to occur.<sup>12</sup> 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 Northeast Woodford District and allocated the \$85,800 revenue increase across the board to Northeast Woodford District'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 \$726,890 Revenue Required from Rates, an approximate 13.38 percent increase. These rates will increase a typical customer's monthly water bill from \$21.86 to \$24.74, an increase of \$2.88, or approximately 13.18 percent.<sup>13</sup>

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<sup>11</sup> Northeast Woodford District's Response to Staff's First Request, 1f, 1f\_Rate\_Study\_2021.xlsx, Revenue Requirement Tab.

<sup>12</sup> Northeast Woodford District's Responses to Staff's First Request, Item 10.

<sup>13</sup>  $\$24.74$  (Average Bill New Water Rates) -  $\$21.86$  (Average Bill Current Water Rates) =  $\$2.88$   
(Total Difference in Customer Bill)  $\div$   $\$21.86$  (Average Bill Current Water Rates) = 13.18%

3. Nonrecurring Charges. Following the Commission's recent decisions,<sup>14</sup> Commission Staff has reviewed Northeast Woodford District's Nonrecurring Charges. The Commission found that because 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. Northeast Woodford District provided the cost justification information for the nonrecurring charges and updated the information with a filing on October 24, 2022.<sup>15</sup> Commission Staff reviewed the cost justification information provided by Northeast Woodford District and have adjusted the charges performed by utility personnel, by removing Field Labor Costs and Office/Clerical Labor Costs that occur during normal business hours from the charges. Commission Staff adjusted the mileage rate to the current allowable mileage rate determined by the Internal Revenue Service (IRS) in the amount of \$0.625 per mile.<sup>16</sup> The Reconnection Charge is performed by Contract Labor<sup>17</sup> and has been adjusted based on updated cost justification information and the current IRS mileage allowance.<sup>18</sup> Northeast Woodford District's bank does not charge a fee for returned checks, so Commission Staff removed labor costs as discussed above, and adjusted the Returned

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<sup>14</sup> 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).

<sup>15</sup> Northeast Woodford District's Responses to Staff's First Request, Item 3-4, and updated filing of October 24, 2022.

<sup>16</sup> <https://www.irs.gov/newsroom/irs-issues-standard-mileage-rates-for-2022>.

<sup>17</sup> Northeast Woodford District's Responses to Staff's First Request, Item 6b.

<sup>18</sup> Northeast Woodford District's Responses to Staff's First Request, Item 4.

Check Fee accordingly by allowing the cost of the supplies to manage such occurrences.<sup>19</sup> Commission Staff accepts Northeast Woodford District's proposed Meter Deposit charge as filed.<sup>20</sup> Such adjustments result in the following revised Nonrecurring Charges:

| <u>Nonrecurring Charge</u> | <u>Current Tariff</u> | <u>Revised Charge</u>  |
|----------------------------|-----------------------|------------------------|
| Reconnection Fee           | \$ 70.00              | \$ 69.00 <sup>21</sup> |
| Returned Check Fee         | 30.00                 | 5.00                   |
| Meter Deposit              | 21.16                 | 26.62                  |

The adjustments to the Nonrecurring Charges result in a decrease in Other Operating Revenue of (\$35) as shown below. Commission Staff recommends that the Commission order Northeast Woodford District to adjust its Nonrecurring Charges to those found in the Appendix to this report.

|                                   | <u>Occurrences</u> | <u>Other Water Revenue</u> | <u>Adjustment</u> | <u>Pro Forma</u> |
|-----------------------------------|--------------------|----------------------------|-------------------|------------------|
| Reconnection Charge <sup>22</sup> | 35                 | \$2,450.00                 | (\$35.00)         | \$2,415.00       |

<sup>19</sup> Northeast Woodford District's Responses to Staff's First Request, Item 4.

<sup>20</sup> Northeast Woodford District's Responses to Staff's First Request, Item 4.

<sup>21</sup>

| <u>Reconnection Fee/ Turn-On Charge</u> |             |               |                       |                    |
|---|-------------|---------------|-----------------------|--------------------|
|   | <u>Rate</u> | <u>Amount</u> | <u>Utility Charge</u> | <u>PSC Allowed</u> |
| Field Expense- Labor                    | 42.00       | 0.83          | \$ 35.00              | 35.00              |
| Clerical Supplies                       | 0.6         | 1             | 0.60                  | 0.60               |
| Clerical Labor                          | 15          | 1             | 15.00                 | 15.00              |
| Transportation                          | 0.625       | 30            | 15.00                 | 18.75              |
|   |             |               | 65.60                 | 69.00              |

<sup>22</sup> Northeast Woodford District's Correction to Response to Staff's First Request, Item 3.

Northeast Woodford District provided the Average Meter Connection Expense Cost Justification forms for a 5/8- X 3/4-Inch meter and a 1 Inch meter.<sup>23</sup> Northeast Woodford District's Cost Justification forms indicates that it should increase its 5/8- X 3/4-inch meter connection fee by \$523 from \$844 to \$1367; and should increase its 1 inch meter connection fee by \$633 from \$1,035 to \$1668, in order to reflect the current costs to install a meter. Staff recommends that an increase is reasonable to recover the increased cost to install a 5/8 X 3/4 inch meter. Staff also recommends that an increase is reasonable to recover the increased cost to install a 1 inch meter.

4. Accounting Software. Northeast Woodford District provided an Excel general ledger recap that records monthly subtotals and a combined yearly total instead of a formal General Ledger.<sup>24</sup> In Commission Staff's Second Request for Information (Staff's Second Request) Northeast Woodford District stated they compiled the data from the recap and that the "Operation and Maintenance" spreadsheet is essentially an electronic version of a ledger book.<sup>25</sup> This created several difficulties for Commission Staff when it attempted to analyze the financial records of Northeast Woodford District. Without the General Ledger, Commission Staff was unable to verify account balances or transactions. Therefore, Commission Staff recommends that the Commission require Northeast Woodford District to obtain accounting software and follow the Uniform System of Accounts for Class A/B Water Systems (USoA).

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<sup>23</sup> Northeast Woodford District's Response to Commission Staff's First Request, Item 4.

<sup>24</sup> Northeast Woodford District's Response to Staff's First Request, Item 1a; 1a\_General\_Ledger\_2021.xlsx.

<sup>25</sup> Northeast Woodford District's Response to Commission Staff's Second Request for Information (Staff's Second Request), (filed October 10, 2022), Item 1.

## PRO FORMA OPERATING STATEMENT

Northeast Woodford District's Pro Forma Operating Statement for the test year ended December 31, 2021, as determined by Commission Staff, appears below.

|   | <u>Test Year</u> | <u>Adjustment</u> | <u>(Ref.)</u> | <u>Pro Forma</u> |
|---|------------------|-------------------|---------------|------------------|
| <b>Operating Revenues</b>                       |                  |                   |               |                  |
| Total Metered Water Sales                       | 643,769          | (2,679)           | (A)           | 641,090          |
| <b>Other Water Revenues</b>                     |                  |                   |               |                  |
| Forfeited Discounts                             | 10,925           | 3,451             | (B)           | 14,376           |
| Misc. Service Revenues                          | 2,450            | (35)              | (C)           | 2,415            |
| <b>Total Operating Revenues</b>                 | <b>657,144</b>   | <b>737</b>        |               | <b>657,881</b>   |
| <b>Operating Expenses</b>                       |                  |                   |               |                  |
| <b>Operation and Maintenance Expenses</b>       |                  |                   |               |                  |
| Salaries and Wages - Employees                  | 18,200           | (18,200)          | (D)           | -                |
| Salaries and Wages - Officers                   |                  |                   |               | -                |
| Employee Pensions and Benefits                  |                  |                   |               |                  |
| Purchased Water                                 | 419,713          |                   |               | 419,713          |
| Purchased Power                                 | 10,572           |                   |               | 10,572           |
| Materials and Supplies                          | 23,375           |                   |               | 23,375           |
| Contractual Services- Accounting                | 8,200            |                   |               | 8,200            |
| Contractual Services- Management Fees           | 38,787           |                   |               | 38,787           |
| Contractual Services- Other                     | 51,160           | (5,244)           | (E)           | 45,916           |
| Insurance- General Liability                    | 5,560            |                   |               | 5,560            |
| Miscellaneous Expense                           | 11,293           |                   |               | 11,293           |
| <b>Total Operation and Maintenance Expenses</b> | 586,860          | (23,444)          |               | 563,416          |
| Depreciation                                    | 66,676           | 7,594             | (F)           |                  |
|   |                  | 123               | (G)           | 74,393           |
| Taxes Other Than Income                         | 2,738            | (1,392)           | (D)           | 1,346            |
| <b>Utility Operating Expenses</b>               | <b>656,274</b>   | <b>(17,119)</b>   |               | <b>639,155</b>   |
| <b>Net Operating Income</b>                     | 870              | 17,856            |               | 18,726           |
| Interest and Dividend Income                    | 2,204            |                   |               | 2,204            |
| <b>Income Available to Service Debt</b>         | <b>\$ 3,074</b>  | <b>\$ 17,856</b>  |               | <b>\$ 20,930</b> |

(A) Billing Analysis Adjustment. Northeast Woodford District proposed an adjustment of \$2,679 to decrease Total Metered Water Sales.<sup>26</sup> Northeast Woodford District provided a billing analysis listing the water usage and water sales revenue for the 12-month test year in its application, subtracting billing adjustments of \$29,865,<sup>27</sup> with net metered water sales revenue reported as \$641,090.<sup>28</sup> According to Northeast Woodford District’s 2021 Annual Report, the total metered water sales revenue reported for the test year is \$643,769.<sup>29</sup> Northeast Woodford District provided usage data,<sup>30</sup> and billing adjustment information<sup>31</sup> to which Commission Staff calculated a normalized revenue amount based on the statistics compiled in the table below, which includes net billing adjustments<sup>32</sup> and agrees with North Woodford District’s normalized revenue of \$641,090. Accordingly, Commission Staff decreased test year water sales by \$2,679 to reflect the adjustment.

| Meter Size                   | Bills  | Gallons Sold | Revenue   |
|------------------------------|--------|--------------|-----------|
| 5/8 inch                     | 11,903 | 141,485,000  | \$633,137 |
| Fayette Co                   | 300    | 3,053,000    | 13,960    |
| 2 inch                       | 36     | 5,918,000    | 23,857    |
| Totals                       |        |              | 670,955   |
| Less: Billing Adjustments    |        |              | (29,865)  |
| Pro Forma Normalized Revenue |        |              | 641,090   |

<sup>26</sup> Application, Attachment 5, Schedule of Adjusted Operations, Adjustment A.

<sup>27</sup> Northeast Woodford District’s Response to Staff’s First Request, Item 19\_Adjustments\_2021.pdf.

<sup>28</sup> Application, Attachment 5, Schedule of Adjusted Operations.

<sup>29</sup> 2021 Annual Report at 49.

<sup>30</sup> Northeast Woodford District’s Response to Staff’s First Request, Item 18d\_2021\_Billing\_Registers\_Totals\_Pages.pdf.

<sup>31</sup> Northeast Woodford District’s Response to Staff’s First Request, Item 18e.

<sup>32</sup> Northeast Woodford District’s Response to Staff’s First Request, Item 18e.

|                                |                         |
|--------------------------------|-------------------------|
| Less: Test Year Revenue        | <u>643,769</u>          |
| Metered Water Sales Adjustment | <u><u>(\$2,679)</u></u> |

(B) Late Payment Revenue. Northeast Woodford District recorded \$10,925 in Forfeited Discount revenue during the test year.<sup>33</sup> North Woodford District had not yet normalized the collection of late payment fees during test year as the moratorium regarding the collection of late payment fees due to the COVID-19 pandemic was in place the prior year. 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.<sup>34</sup> Based upon a three-year average of \$14,376, Commission Staff increased Miscellaneous Service Revenues by \$3,451.

| <u>Year</u>                         | <u>Amount</u>         |
|-------------------------------------|-----------------------|
| 2017                                | \$13,635              |
| 2018                                | 16,584                |
| 2019                                | <u>12,910</u>         |
| Three-Year Average                  | 14,376                |
| Less: Test-Year Forfeited Discounts | <u>(10,925)</u>       |
| Pro Forma Adjustment                | <u><u>\$3,451</u></u> |

(C) Miscellaneous Service Revenue. Northeast Woodford District listed test-year Other Water Revenues of \$13,375, which included \$10,925 of Late Payment Penalties,<sup>35</sup> and \$2,450 of Reconnection fees.<sup>36</sup> Northeast Woodford District provided

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<sup>33</sup> Northeast Woodford District's Response to Staff's Second Request, Item 4\_Penalties\_2021.

<sup>34</sup> Northeast Woodford District's Response to Staff's First Request, Item 2.

<sup>35</sup> Northeast Woodford District's Response to Staff's Second Request, Item 4\_Penalties\_2021.

<sup>36</sup> Northeast Woodford District's Response to Staff's First Request, Item 13.

information about the Nonrecurring Charges revenue,<sup>37</sup> and Commission Staff calculated an adjustment to Other Water Revenue. The adjustment to Nonrecurring Charges results in a decrease to Miscellaneous Service Revenues of \$35 from reconnection fees as discussed above.

(D) Salaries and Wages – Employees and Officers. In its application, Northeast Woodford District proposed to reduce Salaries and Wages – Employees and increase Salaries and Wages – Officers by \$18,200<sup>38</sup> due to Northeast Woodford District mistakenly reporting the Officers' Salaries as Salaries and Wages – Employees.

In response to Commission Staff's request for the fiscal court minutes approving Northeast Woodford District's commission compensation, Northeast Woodford District stated that Woodford County Fiscal Court has not taken any action on Officers' Compensation.<sup>39</sup> Therefore, there is no evidence on record authorizing Officers' Compensation. Commission Staff decreased Salaries and Wages – Employees expense by \$18,200, and Taxes other than Income \$1,392 for payroll taxes to remove the Officers' Salaries and payroll Taxes. Additionally, Commission Staff recommends that the Commission require Northeast Woodford District to seek fiscal court approval for the Officers' Salaries at the next session back to the date it began to pay current Officers' salaries to the extent allowed by law.

(E) Expenses Related to Meter Installations. In its application, Northeast Woodford District proposed an adjustment to decrease Contractual Services – Other by

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<sup>37</sup> Northeast Woodford District's Response to Staff's First Request, Item 13.

<sup>38</sup> Application, Attachment 4, Statement of Adjusted Operations, Adjustment B.

<sup>39</sup> Northeast Woodford District's Response to Staff's Second Request, Item 3.

\$5,244 to account for the reduction of the capital costs of the installation of new water connections.<sup>40</sup> During the test year, Northeast Woodford District installed four new water connections and had an additional charge for work required to install one of the meters.<sup>41</sup> The USoA requires that these costs be capitalized as Utility Plant in Service and depreciated over their estimated useful lives.<sup>42</sup> Therefore, Commission Staff agrees with Northeast Woodford District's proposed adjustment and reduced Contractual Services – Other by \$5,244. In addition, Commission Staff has capitalized the costs and made a corresponding adjustment to test-year depreciation as shown in adjustment (G).

(F) Depreciation Expense. In its application, Northeast Woodford District proposed to increase its test year Depreciation Expense of \$66,676 by \$7,679<sup>43</sup> 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.<sup>44</sup> Northeast Woodford District proposed to follow this methodology to calculate its Depreciation Expense.

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<sup>40</sup> Application, Attachment 4, Statement of Adjusted Operations, Adjustment C.

<sup>41</sup> Correction to response to Request for Information #1 Question #5 (filed Nov 2, 2022), [Read\\_First\\_Letter\\_Correcting\\_Response\\_to\\_RFI\\_1\\_Question\\_5.pdf](#).

<sup>42</sup> USoA, Accounting Instruction 19 and 33.

<sup>43</sup> Northeast Woodford District's Response to Staff's First Request, Item 1f, [1f\\_Rate\\_Study\\_2021.xlsx](#), Adjustment D.

<sup>44</sup> Case No. 2020-00290, *Electronic Application of Bluegrass Water Utility Operating Company, LLC for an Adjustment of Rates and Approval of Construction* (Ky. PSC Aug. 2, 2021), Order at 53; see also Case No. 2020-00195, *Electronic Application of Southeast Daviess County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020), Order.

During its analysis, Commission Staff determined that the service life used by Northeast Woodford District for a few of the assets did not match the applicable midpoint of the NARUC ranges. Commission Staff found no evidence to support depreciable lives that vary from the midpoints of the NARUC ranges. Therefore, Commission Staff recommends recalculating Northeast Woodford District's depreciation based on the applicable midpoints of the NARUC ranges, which will increase Northeast Woodford District's Depreciation Expense by \$7,594 to \$74,270 as shown below.

| Categories                        | Test Year<br>Depreciation | Depreciation<br>Adjustment | Pro Forma<br>Depreciation |
|-----------------------------------|---------------------------|----------------------------|---------------------------|
| General Plant                     | \$1,537                   | \$(301)                    | \$1,236                   |
| Pumping Plant                     | 3,577                     | 129                        | 3,706                     |
| Transmission & Distribution Mains | 25,709                    | (827)                      | 24,882                    |
| Meter Installation                | 205                       | (20)                       | 185                       |
| Meter Change-Outs                 | 8,227                     | 13,325                     | 21,551                    |
| Tank Fence                        | 200                       | (147)                      | 53                        |
| Reservoirs & Tanks                | 24,391                    | (5,508)                    | 18,884                    |
| Tank Painting & Repairs           | 2,830                     | 943                        | 3,773                     |
| Total                             | \$66,676                  | \$7,594                    | \$74,270                  |

(G) Capitalization of Test-Year Water Connections. As explained in adjustment (E) above, the expenses related to the installation of new water connections are capital expenditures that should be capitalized as Utility Plant in Service and depreciated over their estimated useful lives. Therefore, Commission Staff calculated the annual depreciation amount for the test year and increased depreciation expense by \$123 as shown below.

|   |         |
|---|---------|
| Test-Year Water Connections Expense           | \$5,244 |
| Divided by: Useful Service Life of 42.5 Years | 42.5    |
| Pro Forma Depreciation Adjustment             | \$123   |

## OVERALL REVENUE REQUIREMENT AND REQUIRED REVENUE INCREASE

The Operating Ratio methodology<sup>45</sup> is used when there is no basis for a rate of return determination, the cost of the utility has fully or largely been funded through contributions, or there is little or no outstanding long-term debt. Commission Staff is of the opinion that an operating ratio of 88 percent will allow Northeast Woodford District sufficient revenues to cover its reasonable operating expenses and provide for reasonable equity growth. Therefore, Commission Staff finds the Operating Ratio method is more appropriate as Northeast Woodford District has only two outstanding debts.

By applying the Operating Ratio method, Commission Staff found Northeast Woodford District's Revenue Requirement from Rates for Service to be \$726,890. A revenue increase of \$85,800, or 13.38 percent, is necessary to generate the Overall Revenue Requirement.

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<sup>45</sup> Operating Ratio is defined as the ratio of expenses, including depreciation and taxes, to gross revenues. It is illustrated by the following equation:

$$\text{Operating Ratio} = \frac{\text{Operating Expenses} + \text{Depreciation} + \text{Taxes}}{\text{Gross Revenues}}$$

|   | Northeast Woodford<br>Water District | Staff               |
|---|--------------------------------------|---------------------|
| Pro Forma Operating Expenses              | \$ 658,709                           | \$ 639,155          |
| Divided by: Operating Ratio               | <u>88%</u>                           | <u>88%</u>          |
| Subtotal                                  | 748,533                              | 726,313             |
| Plus: Interest Expense                    | <u>20,339</u>                        | <u>19,572</u> (1)   |
| Total Revenue Requirement                 | 768,872                              | 745,885             |
| Less: Other Operating Revenue             | (13,375)                             | (16,791)            |
| Interest Income                           | <u>(2,204)</u>                       | <u>(2,204)</u>      |
| Revenue Required From Water Sales         | 753,293                              | \$ 726,890          |
| Less: Revenue from Sales at Present Rates | <u>(641,090)</u>                     | <u>\$ (641,090)</u> |
| Required Revenue Increase                 | <u>\$ 112,204</u>                    | <u>\$ 85,800</u>    |
| Percentage Increase                       | <u>17.50%</u>                        | <u>13.38%</u>       |

1. Average Annual Interest and Fees Payments. At the time of Commission Staff's review, Northeast Woodford District had one outstanding United States Department of Agriculture, Rural Development (RD) promissory notes, and one outstanding KIA Loan. Northeast Woodford District filed an updated calculation for the average annual Interest and fees of \$20,339.<sup>46</sup> Northeast Woodford District requested recovery of the average annual interest on its indebtedness based on a five-year average of the annual interest and fee payments for the years 2022 through 2026.<sup>47</sup> However, because the statutory date for a final Order to be issued in this proceeding is May 19, 2023, the 2022 payments will be recovered through Northeast Woodford District's existing rates. Therefore, only Debt Service payments that will be made after the new rates are placed into effect should be considered in determining Northeast Woodford District's Annual Interest and Fees expense. Commission Staff calculated the average annual

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<sup>46</sup> Northeast Woodford District's Response to Staff's First Request, Item 11.

<sup>47</sup> Northeast Woodford District's Response to Staff's First Request, Item 1f, 1f\_Rate\_Study\_2021.xlsx, Adjustment D.

principal and interest on a five-year average for the years 2023 through 2027. As shown below, Commission Staff calculated an Average Interest and Fees of \$19,572.

| 2023-2027 Interest & Fees |                  |                   |       |                 |
|---------------------------|------------------|-------------------|-------|-----------------|
| Year                      | RD Bond Interest | KIA Loan Interest | Fees  | Total           |
| 2023                      | \$15,151         | \$6,779           | \$775 | \$22,705        |
| 2024                      | 14,001           | 6,480             | 741   | 21,222          |
| 2025                      | 12,765           | 6,176             | 706   | 19,647          |
| 2026                      | 11,471           | 5,866             | 670   | 18,008          |
| 2027                      | 10,091           | 5,551             | 634   | 16,277          |
| Total                     |                  |                   |       | 97,858          |
| Divide by 5 Years         |                  |                   |       | <u>5</u>        |
| Average Annual Interest   |                  |                   |       | <u>\$19,572</u> |

Signatures

/s/ William M. Foley

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

/s/Elizabeth Stefanski

Prepared by: Elizabeth Stefanski  
Rate Design Branch  
Division of Financial Analysis

APPENDIX

APPENDIX TO COMMISSION STAFF'S REPORT OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2022-00221 DATED NOV 21 2022

The following rates and charges are prescribed for the customers in the area served by Northeast Woodford County Water District. 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  | \$ | 14.88 Minimum Bill |
| Next  | 2,000 Gallons  |    | 0.00493 Per Gallon |
| Next  | 6,000 Gallons  |    | 0.00461 Per Gallon |
| Over  | 10,000 Gallons |    | 0.00433 Per Gallon |

2-Inch Meter

|       |                |    |                    |
|-------|----------------|----|--------------------|
| First | 20,000 Gallons | \$ | 96.13 Minimum Bill |
| Over  | 20,000 Gallons |    | 0.00433 Per Gallon |

Nonrecurring Charges

|                                 |    |          |
|---------------------------------|----|----------|
| 5/8- x 3/4-Inch Water Tap On    | \$ | 1,367.00 |
| 1-Inch Water Tap On             |    | 1,668.00 |
| Reconnection Fee/Service Charge |    | 69.00    |
| Returned Check Charge           |    | 5.00     |
| Meter Deposit                   |    | 26.62    |

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