

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF NORTH)	CASE NO.
SHELBY WATER COMPANY FOR A RATE)	2022-00317
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 November 18, 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 November 18, 2022 Order, North Shelby Water Company (North Shelby 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 North Shelby 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 FEB 08 2023

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 NORTH SHELBY WATER COMPANY

North Shelby Water Company (North Shelby Water) is a water utility organized pursuant to KRS Chapter 273 that owns and operates a water distribution system through which it provides retail water service to approximately 5,352 residential customers, 23 commercial customers, 3 industrial customers, 14 public authorities, and 6 public fire protection organizations that reside in Shelby, Franklin, Henry, and Oldham counties, Kentucky.¹ On September 14, 2022, North Shelby Water tendered an application with the Commission requesting to adjust its water rates pursuant to 807 KAR 5:076. After curing deficiencies, North Shelby Water's application was deemed filed as of September 27, 2022. The application was tendered pursuant to the Commission's Order in Case No. 2021-00249, which required North Shelby Water to file an application for an adjustment of its base rates by July 19, 2022.² On July 14, 2022, North Shelby Water

¹ *Annual Report of North Shelby Water to the Public Service Commission for the Calendar Year Ended December 31, 2021* (2021 Annual Report) at 12 and 49.

² Case No. 2021-00249, *Electronic Purchased Water Adjustment Filing of North Shelby Water Company* (Ky. PSC July 19, 2021) at 5.

requested an extension of time to file its application by September 16, 2022.³ The Commission approved the request for the extension by Order entered on August 23, 2022.⁴ North Shelby Water last sought a base rate increase pursuant to the alternative rate filing procedure in Case No. 2009-00484.⁵ Since that matter, North Shelby Water has only adjusted its rates pursuant to purchased water adjustments, financing approval, or in conjunction with an application for a Certificate of Public Convenience and Necessity.

To ensure the orderly review of this application, the Commission established a procedural schedule by Order dated October 14, 2022. Commission Staff's First Request for Information (Staff's First Request) was issued on October 14, 2022, with a response due date of November 3, 2022. North Shelby Water filed a partial response to Staff's First Request on November 10, 2022. As part of the filing, North Shelby Water stated that while it was aware of the November 3, 2022 deadline to respond, its staff experienced illnesses and that completing the responses had "fallen through the cracks." North Shelby Water requested an extension until November 23, 2022, to complete its response to Staff's First Request. On November 18, 2022, the Commission issued an Order with an amended procedural schedule to address the request for additional time. North Shelby Water submitted the remainder of its responses to Staff's First Request on November 22, 2022. Commission Staff's Second Request for Information (Staff's Second Request) was

³ Case No. 2021-00249, *Electronic Purchased Water Adjustment Filing of North Shelby Water Company* (Ky. PSC July 14, 2021).

⁴ Case No. 2021-00249, *Electronic Purchased Water Adjustment Filing of North Shelby Water Company* (Ky. PSC Aug. 23, 2021).

⁵ Case No. 2009-00484, *Application of North Shelby Water Company for Approval of Increase in Rates for Water Service* (Ky. PSC Apr. 15, 2010).

issued on December 5, 2022, and North Shelby Water filed its response to Staff's Second Request on December 22, 2022.

WATER LOSS

The Commission notes that in its 2021 Annual Report, North Shelby Water reported a water loss of 16.6842 percent.⁶ Commission regulation 807 KAR 5:066, Section 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 16.6842 percent water loss, the annual cost of water loss in excess of 15.00 percent is \$23,089 and the total annual cost of water loss to North Shelby Water is \$228,720 as show in the table below.

Total Water Loss	Purchased Water	Purchased Power	Total
Pro Forma Purchases	\$ 1,285,163	\$ 85,713	\$ 1,370,876
Water Loss Percent	16.6842%	16.6842%	
Total	\$ 214,419	\$ 14,301	\$ 228,720

Excess Water Loss	Purchased Water	Purchased Power	Total
Pro Forma Purchases	\$ 1,285,163	\$ 85,713	\$ 1,370,876
Disallowed Percent	1.6842%	1.6842%	
Loss in Excess of Allowed Amount	\$ 21,645	\$ 1,444	\$ 23,089

DISCUSSION

To comply with the requirements of 807 KAR 5:076, Section 9,⁷ North Shelby Water used the calendar year ended December 31, 2021, as the basis for its application.

⁶ 2021 Annual Report at 57.

⁷ The reasonableness of the proposed rates shall be determined using a 12-month historical test period, adjusted for known and measurable changes, that coincides with the reporting period of the applicant's annual report for the immediate past year.

North Shelby Water determined that a base rate revenue increase of \$46,784, or 1.37 percent, was necessary to achieve the revenue requirement as shown in the table below.⁸ North Shelby Water stated that it did not wish to adjust its rates.⁹

Pro Forma Operating Expenses	\$ 3,341,019
Plus: Average Annual Principal and Interest Payments	400,942
Additional Working Capital	80,188
Overall Revenue Requirement	<u>3,822,149</u>
Less: Other Operating Revenue	(368,471)
Other Operating Income	(3,210)
Revenue Required from Rates	<u>3,450,468</u>
Less: Pro Forma Present Rate Service Revenues	(3,403,684)
Required Revenue Increase	<u><u>\$ 46,784</u></u>
Percentage Increase	<u><u>1.37%</u></u>

To determine the reasonableness of the rates requested by North Shelby Water, Commission Staff performed a limited financial review of North Shelby 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 measurable¹⁰ 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.

⁸ Application, Attachment 4, Revenue Requirements Using Debt Service Coverage Method at 14.

⁹ Application, Attachment 2, Reasons for Application.

¹⁰ 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).

Commission Staff's findings are summarized in this report. Jeff Abshire and Noah Abner reviewed the calculation of North Shelby Water's Overall Revenue Requirement and Eddie Beavers reviewed North Shelby Water's reported revenues and rate design.

SUMMARY OF FINDINGS

1. Overall Revenue Requirement and Required Revenue Increase. By applying the Debt Service Coverage (DSC) method, as generally accepted by the Commission, Commission Staff found that North Shelby Water's required revenue from water sales is \$3,508,653 to meet the Overall Revenue Requirement of \$3,852,542 and that a \$73,756 revenue increase, or 2.15 percent, to pro forma present rate revenues is necessary to generate the Overall Revenue Requirement.

2. Monthly Water Service Rates. North Shelby Water stated that it did not wish to increase its rates.¹¹ North Shelby Water has not performed a cost of service study (COSS). North Shelby Water stated that it did not complete a COSS at this time as there have been no material changes in the water system.¹²

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 has followed the method previously accepted by the Commission and has allocated the

¹¹ Application, Attachment 2, Reasons for Application.

¹² North Shelby Water's Response to Commission Staff's First Request (filed Nov. 10, 2022), Item 15d.

\$73,756 revenue increase evenly across the board to North Shelby 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 \$3,508,653 for Revenue Required from Rates, an approximate 2.15 percent increase. These rates will increase a typical residential customer's monthly water bill from \$47.35 to \$48.37, an increase of \$1.02, or approximately 2.15 percent.¹³ While North Shelby Water stated that they did not wish to adjust their rates, Commission Staff recommends that the Commission approve the rates as presented in the Appendix. The Commission has an obligation to ensure that utilities receive fair, just and reasonable rates so that utilities can provide reliable service.

3. Nonrecurring Charges. Following the Commission's recent decisions,¹⁴ Commission Staff has reviewed North Shelby Water'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. Commission Staff has

¹³ To determine the typical residential customer's usage, Staff used the 5/8" x 3/4" usage from the Application, Exhibit 5: 323,841,600 gallons divided by 62,990 bills = the typical residential customer usage of approximately 5,140 gallons per month.

¹⁴ 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).

reviewed the most recent cost justification information provided in response to Staff's First Request.¹⁵ Such adjustments result in the following revised nonrecurring charges:

Nonrecurring Charges	
Connection/Turn On Charge	\$12.20
Connection/Turn On Charge After Hours	\$45.00
Inspection of Service Line	\$12.20
Membership Fee	\$5.50
Meter Test Charge	\$12.20
Reconnection Fee	\$12.20
Reconnection Fee After Hours	\$45.00
Returned Check Charge	\$15.00
Service Investigation Charge	\$12.20

Commission Staff followed Commission precedent and made the adjustments to the Nonrecurring Charges, which results in a decrease to the charges and an increase to the total revenue requirement of \$40,044, as shown below.¹⁶

	Num	Current Rate	Total	Revised Rate	Adj	Pro Forma
<i>Miscellaneous Service Revenues</i>						
After Hours	0	\$50.00	0	\$12.20	0	-
Membership Fee	481	\$16.00	7,696	\$5.50	(5,051)	2,646
Meter Test Charge	3	\$85.00	255	\$12.20	(218)	37
Returned Check Charge	52	\$15.00	800	\$15.00	(20)	780
Turn-on, Insp Serv Line, Recon Re-reading, Serv Insp, Meter Inv	1,147	\$40.00	48,749	\$12.20	(34,755)	13,994
Total Miscellaneous Service Revenues			<u>\$57,500</u>		<u>(\$40,044)</u>	<u>\$17,456</u>

¹⁵ North Shelby Water's Response to Staff's First Request (filed Nov. 22, 2022), Item 14, 14_Nonrecurring_Charge_Cost_Justification.pdf.

¹⁶ Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020).

PRO FORMA OPERATING STATEMENT

North Shelby Water's Pro Forma Operating Statement for the test year ended December 31, 2021, as determined by Staff, appears below.

	Test Year	Adjustment	(Ref)	Pro Forma
Operating Revenues				
Sales of Water	\$ 3,408,671	\$ 26,226	(A)	\$ 3,434,897
Public Fire Protection	3,210			3,210
Late Payment Penalties	35,435	6,890	(B)	42,325
Miscellaneous Service Revenues	234,423	800	(C)	
		(40,044)	(C)	195,179
Rents from Water Property	85,212			85,212
Other Water Revenues	13,401	(5,393)	(D)	
		(800)	(D)	7,208
Total Operating Revenues	3,780,352	(12,321)		3,768,031
Operating Expenses				
Operation and Maintenance Expenses				
Salaries and Wages - Employees	494,157	14,072	(E)	
		(11,000)	(F)	497,229
Salaries and Wages - Commissioners	36,400	(11,400)	(G)	25,000
Employee Pensions and Benefits	319,128	15,976	(H)	
		(59,831)	(H)	
		10,392	(I)	285,665
Purchased Water	1,262,161	23,002	(J)	
		(21,257)	(J)	1,263,906
Purchased Power for Pumping	85,713	(1,444)	(J)	84,269
Materials and Supplies	259,100			259,100
Contractual Services	71,897			71,897
Transportation Expense	52,186			52,186
Insurance	63,462			63,462
Miscellaneous Expense	40,414			40,414
Total Operation and Maintenance Expenses	2,684,618	(41,490)		2,643,128
Taxes Other Than Income - FICA	54,324	(867)	(K)	53,457
Depreciation	747,182	(72,355)	(L)	674,827
Total Operating Expenses	3,486,124	(114,712)		3,371,412
Net Operating Income	294,228	102,391		396,619
Interest Income	0	13,965	(M)	13,965
Income Available to Service Debt	\$ 294,228	\$ 116,356		\$ 410,584

(A) Billing Analysis Adjustment. North Shelby Water proposed to increase its test-year revenues from retail water sales of \$3,408,671 by \$26,226 to reflect the two

increases in rates made during the year of 2022 due to purchase water adjustments.¹⁷ Commission Staff made adjustments to reflect the rates that are currently being charged per North Shelby Water's tariff on file with the Commission. North Shelby Water's adjustment meets the ratemaking criteria of being known and measurable, and Commission Staff included the adjustment in pro forma operations.

(B) Late Payment Penalties. In its application, North Shelby Water proposed a pro forma amount of \$35,435 for Forfeited Discounts. Commission Staff calculated an average of \$42,325 in late payment penalties based on information provided for 2021 and 2022.¹⁸ Commission Staff increased the pro forma amount by \$6,890.

(C) Miscellaneous Service Revenues. North Shelby Water reported test year Miscellaneous Service Revenues of \$234,423.¹⁹ North Shelby Water provided responses to two rounds of requests for information. In its responses it provided revised information concerning the returned check fee income of \$800 that was reported as Other Water Revenues, which should be reclassified as Miscellaneous Service Revenues.²⁰ As discussed above, nonrecurring charges have been adjusted to remove the labor component. The reduction to nonrecurring charges is \$40,044 for a net reduction by Commission staff to Miscellaneous Service Revenues of \$39,244.

¹⁷ Case No. 2022-00154, *Electronic Purchased Water Adjustment Filing of North Shelby Water Company*, (Ky. PSC July 11, 2022) and Case No. 2022-00225, *Electronic Purchased Water Adjustment Filing of North Shelby Water Company* (Ky. PSC Aug. 22, 2022).

¹⁸ Response to Staff's Second Request (filed Dec. 22, 2022), Item 4, 4_Late_Charges.xlsx. Calculation: 2021 (\$28,840) + 2022 (\$55,810) = \$84,650 ÷ 2 = \$42,325 pro forma amount minus \$35,435 test year = \$6,890.

¹⁹ Application, Item 4, 4_SAO_w_Attachments.pdf.

²⁰ Response to Staff's Second Request, Item 1b.

(D) Other Water Revenues. North Shelby Water reported test year Other Water Revenues of \$13,401.²¹ North Shelby Water stated that returned check fee income of \$800 that was incorrectly classified as Other Water Revenues and should be reclassified to Miscellaneous Service Revenues. Commission Staff identified an additional amount of \$5,393 that does not recur and should be removed.²² Commission Staff decreased Other Water Revenues by a total of \$6,193.

(E) Salaries and Wages - Employees. In its application, North Shelby Water proposed an increase of \$111,637 to Salaries and Wages – Employees expense to reflect increases in wage rates since 2021.²³ North Shelby Water classified a portion of 2021 labor costs to a number of non-salary line-item expenses. However, it did not incorporate these components into its analysis when adjusting salaries for inflation and turnover. Commission Staff reviewed North Shelby Water’s calculations and determined that the proposed adjustment is overstated by \$97,565. Accordingly, Commission Staff increased Salaries and Wages by \$14,072 based on the analysis below.

²¹ Application, Item 4, 4_SAO_w_Attachments.pdf.

²² North Shelby Water’s Response to Staff’s Second Request, Item 1b.

²³ Application, Exhibit C, Statement of Adjusted Operations, References, Adjustment B.

	2_2021_Payroll (11-22-2022)	7_Rate_Study_2 021.xlsx]Wages (11-22-2022)
Primary	565,143.42	579,215.00
Director Fees - Bryan Franklin	7,800.00	0.00
Director Fees - John McGinnis	2,600.00	0.00
Christmas Bonus	11,000.00	11,000.00
Length of Service Bonus	13,252.00	13,252.00
Total for Comparative Reference	599,795.42	603,467.00
Less: Director Fees Included Above	(10,400.00)	0.00
Less: Christmas Bonus	(11,000.00)	(11,000.00)
Adjusted Salaries	578,395.42	592,467.00
Increase		14,071.58

(F) Salaries and Wages – Bonus Payment. North Shelby Water included \$11,000 in the calculation of its pro forma salaries and wages for \$1,000 bonus payments to eleven full-time employees.²⁴

Historically, Commission Staff has not included bonuses or incentive compensation in the calculation of pro forma salaries and wages expense in Commission Staff Reports.²⁵ Additionally, Commission Staff has previously removed expenses for items that would be considered a fringe benefit such as a Christmas dinner or Christmas gift baskets.²⁶ The Attorney General has stated that a water district may only make expenditures that are consistent with its statutory purpose to furnish a water supply.

²⁴ North Shelby Water’s Response to Staff’s First Request (filed Nov. 22, 2022) 7 Rate Study 2021.xlsx {Wages}; and North Shelby Water’s Response to Staff’s Second Request, Item 2.a.

²⁵ See Case No. 2021-00475, *Electronic Application of Carroll County Water District #1 for an Adjustment of Rates Pursuant to 807 KAR 5:076* (Ky. PSC May 17, 2022), Commission Staff’s Report at 11–12; Case No. 2021-00191, *Electronic Application of Grayson County Water District for a Rate Adjustment Pursuant to 807 KAR 5:076* (Ky. PSC Oct. 06, 2021), Commission Staff’s Report at 10.

²⁶ Case No. 2018-00346, *Application of Muhlenberg County Water District #3 for Rate Adjustment for Small Utilities Pursuant to 807 KAR 5:076* (Ky PSC Jan. 22, 2019), Commission Staff’s Report at 11–12.

As a creature of statute, a water district create pursuant to KRS Chapter 74 may expend funds only in keeping with its statutory purpose, or express statutory authorization.²⁷

To expense any part of the funds arising from fees for water services for any purpose other than those for which the district was created is to contravene the provisions contained in sections 171 and 180, State Constitution, and to do so, is illegal. The officer making such illegal expenditure subjects himself to the obligation upon the demand of any citizen who pays fees for water services to either recover from the person to whom the illegal sum was donated or to reimburse the district for the amount of the illegal donation.²⁸

North Shelby Water does not provide evidence in the record to indicate that the bonus payments are a necessary part of employee compensation. Consistent with prior treatment of the calculation of pro forma Salaries and Wages and the Attorney General's opinion, Commission Staff excluded in pro forma operations the bonus payments and corresponding payroll taxes and benefits totaling \$11,000.

(G) Salaries and Wages – Officers. North Shelby Water reported \$36,400 for Salaries and Wages – Officer Expense and did not propose any adjustments. In its Response to Staff's Second Request, North Shelby Water provided the annual compensation for each director totaling \$25,600, which is \$10,800 less than the test year.²⁹ Additionally, in its response to Staff's First Request, North Shelby Water stated that Directors had not attended training during 2021 or year to date 2022.³⁰ One of North Shelby Water's Officer's salary is \$4,200 which exceeds permitted annual compensation

²⁷ OAG 92-43 (Mar 19, 1992).

²⁸ 1956 OAG 36,219.

²⁹ North Shelby Water's Response to Staff's Second Request, 3 Directors Compensation and Expiration.xlsx.

³⁰ North Shelby Water's Response to Staff's First Request (filed Nov. 22, 2022), Item 6.

of \$3,600 by \$600 for an officer who has not received training.³¹ Commission Staff reduced Officer's Salaries by \$11,400 for these items as follows:

Officer	Term Expires	Salary
Herb McCoun	4/30/2023	\$ 3,200
John T McGinnis, Secretary/Treasurer	4/30/2023	3,200
Jim Smith	4/30/2024	2,500
Howard Leo Young	4/30/2024	3,200
Bryan Franklin, President (1)	4/30/2024	4,200
Jimmy Anglin	4/30/2025	3,100
Charles Doane	6/30/2025	3,100
Kevin Armstrong	6/30/2025	3,100
Total Officer Salaries		\$ 25,600
Less: North Shelby Water Submitted Pro Forma		(36,400)
Adjustment to Test Year Salaries		(10,800)
(1) Reduce Allowed Salary to \$3,600		(600)
Total Adjustment		\$ (11,400)

(H) Employee Benefits. In its application, North Shelby Water reported test year Employee Pensions and Benefits of \$319,128 based on its originally filed PSC Annual Report. An amount of \$129,045 for Pension and Other Post-Employment Benefits expense adjustments was not included in this amount; however, North Shelby Water removed the adjustment in its pro forma calculations. The Annual Report was subsequently amended with an increase to benefits of \$129,045 to Pension and OPEB expenses.³²

³¹ KRS 74.020(6), *Appointment of commissioners -- Number -- Terms -- Removal -- Vacancies -- Organization -- Bond -- Compensation -- Mandatory training -- Notice of vacancy* states "Each commissioner shall receive an annual salary of not more than thirty-six hundred dollars (\$3,600), which shall be paid out of the water district fund, except that beginning January 1, 1999, and subject to subsection (9) of this section, each commissioner who completes during an educational year a minimum of six (6) instructional hours of water district management training approved by the Public Service Commission may receive an annual salary of not more than six thousand dollars (\$6,000) to be paid out of the water district fund."

³² North Shelby Water's Response to Staff's First Request (filed Nov. 22, 2022), updated.pdf, Item 18.

North Shelby Water pays 100 percent of its full-time employees' health, dental, and vision insurance premiums. North Shelby Water adjusted the level of employer-funded premiums to be consistent with the Bureau of Labor Statistics' (BLS) national average for an employer's share of health insurance premiums. North Shelby Water adjusted the premium cost to reflect a 79 percent employer contribution for single coverage and 66 percent for family coverage. North Shelby Water also adjusted the employer contribution for dental coverage to 60 percent.³³ In its application, North Shelby Water proposed a reduction of \$45,757 to reflect the employees' share based on the BLS national average. Commission Staff reviewed North Shelby Water's calculations and determined the adjustment should be \$59,831.³⁴ Accordingly, Commission Staff decreased Employee Benefits by \$59,831.

A summary of the adjusted pro forma medical and pension benefit amounts net of the BLS adjustment and compared to North Shelby Water's pro forma total is as follows:

Benefit Descriptions	Test Year Reported by North Shelby	Inflation / Turnover	New Cost	Bureau of Labor Statistics Adjust,emt	Proforma
Medical	\$ 169,851	\$ 15,976	\$ 185,827	\$ (59,831)	\$ 125,996
Pension Contribution	149,277	10,392	159,669	n/a	159,669
Total Benefits	\$ 319,128	\$ 26,368	\$ 345,496	\$ (59,831)	\$ 285,665
North Shelby Water Application					(158,310)
Difference					\$ 127,355

³³ Application, Attachment 4, Statement of Adjusted Operations, References, Adjustment E.

³⁴ Response to Commission Staff's First Request, "3 2021 Medical Benefits.xlsx", Sheet1 at cell "CW85".

A summary of North Shelby Water’s proposed pro forma adjustments, Commission Staff’s adjustments, and the net differences is as follows:

Adjustment Descriptions	North Shelby	Commission	Difference
	Water	Staff	
Increased Pension Cost on Wage Increase	\$ 14,826	\$ 10,392	\$ (4,434)
Remove Non-Cash Pension (1)	(129,887)	0	129,887
Bureau of Labor Statistics Adjustment	(45,757)	(59,831)	(14,074)
Medical Inflation		15,976	15,976
Total Adjustments	<u>\$ (160,818)</u>	<u>\$ (33,463)</u>	<u>\$ 127,355</u>
Pro Forma Balance	<u>\$ 158,310</u>	<u>\$ 285,665</u>	<u>\$ 127,355</u>

(1) North Shelby Water reduced expense for non-cash pension which was not included in their test year amount.

(I) County Employees’ Retirement System. Regular, full-time employees of North Shelby Water are provided with retirement benefits through the County Employees’ Retirement System (CERS), which is administered by the Kentucky Public Pensions Authority. As part of CERS, North Shelby Water makes contributions to employees’ retirement accounts based on annual salaries and wages. The CERS pension expense North Shelby Water reported in the test year conformed to the requirements of the Governmental Accounting Standards Board Statement No. 68 and No. 75 (GASB 68 and 75). In its application, North Shelby Water proposed to increase Employee Pensions and Benefits by \$14,826 to normalize expenses related to CERS contributions to the amount actually paid by North Shelby Water in the test period and to remove the effects of the journal entries made to conform to the requirements of GASB 68 and 75.³⁵

In Case No. 2016-00163,³⁶ Staff discussed in detail how reporting requirements for GASB 68 would affect a utility’s income statement and balance sheet. In that

³⁵ Application, Attachment 4, Statement of Adjusted Operations, References, Adjustment D.

³⁶ Case No. 2016-00163, *Alternative Rate Adjustment Filing of Marion County Water District* (Ky. PSC Aug. 11, 2016), Commission Staff’s Report on Marion County Water District at 11–27.

proceeding, Staff found that the annual pension expense should be equal to the amount of a district's contributions to CERS, which historically have been fairly constant.³⁷ Commission Staff recalculated the pension contribution based on adjusted salaries and determined the increase should be \$10,392 as presented in the benefits adjustment table above.

(J) Water Loss. In its application, North Shelby Water proposed a decrease to Purchased Water Expense of \$21,257 to account for the district's water loss in excess of 15 percent.³⁸ In addition, North Shelby Water proposed a net decrease of \$1,444 to Purchased Power to reflect the disallowance of Purchase Power Expense attributable to water loss above 15 percent.³⁹ Commission Staff agrees with North Shelby Water's proposed adjustments and included \$21,257 in Purchased Water Expense and \$1,444 in Purchased Power Expense as reductions, respectively. Commission Staff identified two Purchased Water Adjustments that were approved during 2022 that were not reflected in North Shelby Water's Schedule of Adjusted Operations.⁴⁰ Commission Staff increased purchased water cost by \$23,002 to reflect the cost effect of the purchased water adjustments.⁴¹

³⁷ Case No. 2016-00163, Aug. 11, 2016 Commission Staff's Report on Marion County Water District at 26.

³⁸ Application, Attachment 4, Statement of Adjusted Operations, References, Adjustment F.

³⁹ Application, Attachment 4, Statement of Adjusted Operations, References, Adjustment F.

⁴⁰ Case No. 2022-0054, *Electronic Purchased Water Adjustment Filing Of North Shelby Water Company* (Ky. PSC July 1, 2022); and Case No. 2022-00225, *Electronic Purchased Water Adjustment Filing of North Shelby Water Company* (Ky. PSC July 19, 2022).

⁴¹ Test Year Purchased Power Expense \$1,158,790 / Gallons Purchased in Test Period 413,582.2 = Average Cost per 1,000 gallons \$2.80.

(K) Taxes other than Income - FICA. North Shelby Water proposed to decrease Taxes Other than Income by \$867. Commission Staff agrees that North Shelby Water's revised adjustment is reasonable and included the \$867 reduction in pro forma operations.

(L) Depreciation Expense. In its application, North Shelby Water reported test year Depreciation Expense of \$747,182.⁴² North Shelby Water decreased its test year depreciation by \$72,355 to reflect adjustments of asset service lives to the midpoint of service life range set forth in the National Association of Regulatory Utility Commissioners (NARUC) publication titled, *Depreciation Practices for Small Water Utilities* (NARUC Study). 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 outside the NARUC ranges, the Commission has historically used the midpoint of the NARUC ranges to depreciate the utility plant. In this proceeding, Commission Staff found no evidence to support depreciable lives that vary significantly from the midpoint of the NARUC ranges. Therefore, Commission Staff agrees with North Shelby Water's proposed adjustment and decreased pro forma Depreciation Expense \$72,355 accordingly.

(M) Interest Income. North Shelby Water did not report interest income in its application. In its response to Staff's First Request, North Shelby Water stated that \$13,965 of interest income was erroneously not included from its Schedule of Adjusted

⁴² Application, ARF-SAO.pdf.

Operations or its Revenue Requirements Schedule.⁴³ Commission Staff added \$13,965 to the pro forma interest income.

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) recovery of depreciation expense, a non-cash item, to provide working capital;⁴⁴ (3) the average annual principal and interest payments on all long-term debts; and (4) working capital that is in addition to depreciation expense.

	North Shelby Water	Commission Staff
Pro Forma Operating Expenses	\$ 3,341,019	\$ 3,371,412
Plus: Average Annual Principal and Interest Payments	400,942	400,942
Additional Working Capital	80,188	80,188
Overall Revenue Requirement	3,822,149	3,852,542
Less: Other Operating Revenue	(368,471)	(329,924)
Other Operating Income	(3,210)	0
Interest Income	0	(13,965)
Revenue Required from Rates	3,450,468	3,508,653
Less: Pro Forma Present Rate Service Revenues	(3,403,684)	(3,434,897)
Required Revenue Increase	\$ 46,784	\$ 73,756
Percentage Increase	1.37%	2.15%

⁴³ North Shelby Water’s Response to Staff’s First Request (filed Nov. 22, 2022), Item 7c.

⁴⁴ 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).

1. Average Annual Principal and Interest Payments. At the time of Commission Staff's review, North Shelby Water had four outstanding loans from the United States Department of Agriculture Rural Development (RD) and three outstanding loans from the National Rural Water Association (NRWA).⁴⁵ North Shelby Water requested recovery of the average annual principal and interest on its indebtedness based on a five-year average of the annual principal, and interest and fee payments for the years 2022 through 2026.⁴⁶ Commission Staff agrees with the methodology North Shelby Water proposed and included \$400,942 in the calculation of the revenue requirement.

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. In its revised exhibits, North Shelby Water requested recovery of an allowance for working capital that is equal to 120 percent of its average annual debt payments for its long-term debt with the RD and NRWA at the time of its application.⁴⁷ RD requires that North Shelby Water charge rates that produce net revenues that are at least 120 percent of its average annual debt payments. Following the Commission's historic practice of including additional working capital, \$80,188 is included in the revenue requirement.

⁴⁵ Case 2016-00255, *Application of North Shelby Water Company for a Certificate of Public Convenience and Necessity and to Incur Indebtedness of \$100,000 for the Purchase of Metering System.*

⁴⁶ Application, Table B, Debt Service Schedule at 17.

⁴⁷ Application, Table B, Debt Service Schedule at 17.

Signatures

/s/ Jeff Abshire

Prepared by: Jeff Abshire
Revenue Requirement Branch
Division of Financial Analysis

/s/ Noah Abner

Prepared by: Noah Abner
Revenue Requirement Branch
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/s/ Eddie Beavers

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Rate Design Branch
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APPENDIX

APPENDIX TO COMMISSION STAFF'S REPORT OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2022-00317 DATED FEB 08 2023

The following rates and charges are prescribed for the customers in the area served by North Shelby Water Company. 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	\$	23.51	Minimum Bill
Next	3,000 Gallons		0.00798	Per 1,000 Gallons
Next	5,000 Gallons		0.00657	Per 1,000 Gallons
Next	40,000 Gallons		0.00586	Per 1,000 Gallons
Over	50,000 Gallons		0.00517	Per 1,000 Gallons

1-Inch Meter

First	5,000 Gallons	\$	47.45	Minimum Bill
Next	5,000 Gallons		0.00657	Per 1,000 Gallons
Next	40,000 Gallons		0.00586	Per 1,000 Gallons
Over	50,000 Gallons		0.00517	Per 1,000 Gallons

1 1/2-Inch Meter

First	10,000 Gallons	\$	80.30	Minimum Bill
Next	40,000 Gallons		0.00586	Per 1,000 Gallons
Over	50,000 Gallons		0.00517	Per 1,000 Gallons

2-Inch Meter

First	15,000 Gallons	\$	109.60	Minimum Bill
Next	35,000 Gallons		0.00586	Per 1,000 Gallons
Over	50,000 Gallons		0.00517	Per 1,000 Gallons

3-Inch Meter

First	35,000 Gallons	\$	226.80	Minimum Bill
Next	15,000 Gallons		0.00586	Per 1,000 Gallons
Over	50,000 Gallons		0.00517	Per 1,000 Gallons

Nonrecurring Charges

Connection/Turn On Charge	\$12.20
Connection/Turn On Charge After Hours	\$45.00
Inspection of Service Line	\$12.20
Membership Fee	\$5.50
Meter Test Charge	\$12.20
Reconnection Fee	\$12.20
Reconnection Fee After Hours	\$45.00
Returned Check Charge	\$15.00
Service Investigation Charge	\$12.20
5/8- x 3/4-Inch Tap Fee	\$1,000.00
1-Inch Tap Fee	\$1,275.00

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