

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF SOUTHERN)	
WATER AND SEWER DISTRICT FOR AN)	CASE NO.
ALTERNATIVE RATE ADJUSTMENT PURSUANT)	2024-00251
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 January 16, 2025, as amended by Order entered April 23, 2025, the attached report containing the recommendations 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 January 16, 2025, Order, Southern Water and Sewer District (Southern District) is required to file written comments regarding the recommendations of Commission Staff no later than 14 days from the date of service of this report. The Commission directs Southern District 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 JUN 16 2025

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 SOUTHERN WATER AND SEWER DISTRICT

Southern Water and Sewer District (Southern District) is a water utility organized pursuant to KRS Chapter 74 that owns and operates a distribution system through which it provides retail water service to approximately 5,210 residential customers and 205 commercial customers, that reside in Floyd County, Kentucky.¹

On December 26, 2024,² Southern District filed its application with the Commission requesting an adjustment to its water service rates pursuant to 807 KAR 5:076. To comply with the requirements of 807 KAR 5:076, Section 9,³ Southern District used the calendar year ended December 31, 2023, as the basis for its application. Southern District's last base rate increase, also filed pursuant to the alternative rate filing procedure,

¹ *Annual Report of Southern Water and Sewer District, Inc. to the Public Service Commission for the Calendar Year Ended December 31, 2023* (2023 Annual Report) at 12 and 49.

² Southern District tendered its application on September 25, 2024. By letter dated September 27, 2024, the Commission rejected the application for filing deficiencies. The deficiencies were subsequently cured, and the application is deemed filed on December 26, 2024.

³ 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.

was in Case No. 2022-00099.⁴ Since that matter, Southern District has only adjusted its rates pursuant to an emergency relief filing pursuant to KRS 278.170.⁵ To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated January 16, 2025. During the pendency of the case, Southern District experienced flooding that extensively damaged its distribution system. This understandably contributed to delays in filing and incomplete information provided by Southern District in response to Staff's requests for information; therefore, the Commission issued an Order on April 23, 2025, modifying the procedural schedule as well as requesting additional information.⁶

Southern District responded to three requests for information from Commission Staff and made three supplemental filings.⁷ Southern District noted in its response to Commission Staff's First Request for Information (Staff's First Request) that, while staff had worked diligently to prepare responses, it had significant challenges that resulted from recent flooding. It further stated that had been challenged by a disruption to access to its accounting records due to the failure of a file server at its accountant's office.⁸

⁴ Case No. 2022-00099, *Electronic Application of Southern Water and Sewer District for an Alternative Rate Adjustment* (Ky. PSC, Dec. 20, 2022).

⁵ Case No. 2022-00300, *Electronic Application of Southern Water and Sewer District for Emergency Relief Pursuant to KRS 278.170* (Ky. PSC Sep. 1, 2022).

⁶ Amended Procedural Schedule (Ky. PSC Apr. 23, 2025).

⁷ Southern District's Response to Staff's First Request (filed Feb. 25, 2025), with Supplements filed on Mar. 4, 2025 and filed Mar. 11, 2025. Southern District's Response to Commission Staff's Second Request for Information (Staff's Second Request) (filed Apr. 1, 2025) with a supplement filed Apr. 8, 2025. Southern District's Response to Commission Staff's Third Request for Information (Staff's Third Request), (filed May 8, 2025) and a supplement filed May 9, 2025.

⁸ Southern District's Response to Staff's First Request, [Read First Response to RFI 1.pdf](#).

UNACCOUNTED-FOR WATER LOSS

Southern District produces approximately 75 percent of its water⁹ and purchases the remainder from the City of Pikeville and Prestonsburg City's Utilities Commission.¹⁰ The Commission notes that in its 2023 Annual Report, Southern District reported a water loss of 56.6897 percent.¹¹ The Commission also notes that Southern District's water loss was 57.4307 percent¹² and 54.7978 percent,¹³ in 2022 and 2021, respectively. 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.¹⁴ The table below shows that the 2023 total annual cost of water loss to Southern District is \$605,311, while the annual cost of water loss in excess of 15 percent is \$445,147.

⁹ 2023 Annual Report at 57.

¹⁰ 2023 Annual Report at 54.

¹¹ 2023 Annual Report at 57.

¹² *Annual Report of Southern Water and Sewer District, Inc. to the Public Service Commission for the Calendar Year Ended December 31, 2022* (2022 Annual Report) at 57.

¹³ *Annual Report of Southern Water and Sewer District, Inc. to the Public Service Commission for the Calendar Year Ended December 31, 2021* (2021 Annual Report) at 57.

¹⁴ [Title 807 Chapter 5 Regulation 066 • Kentucky Administrative Regulations • Legislative Research Commission](#), 807 KAR 5:066, Section 6(3).

Total Water Loss

Description	Purchased Water	Purchased Power	Purchased Chemicals	Total
Pro Forma Purchases	\$ 391,835	\$ 412,500	\$ 263,427	\$ 1,067,762
Water Loss Percent	56.6897%	56.6897%	56.6897%	56.6897%
Total	\$ 222,130	\$ 233,845	\$ 149,336	\$ 605,311

Disallowed Water Loss

Description	Purchased Water	Purchased Power	Purchased Chemicals	Total
Pro Forma Purchases	\$ 391,835	\$ 412,500	\$ 263,427	\$ 1,067,762
Water Loss in Excess of 15%	41.6897%	41.6897%	41.6897%	41.6897%
Total	\$ 163,355	\$ 171,970	\$ 109,822	\$ 445,147

The Commission is placing greater emphasis on monitoring utilities that consistently exceed the 15 percent unaccounted-for water loss.¹⁵ Southern District was approved for a \$5.25 per customer per month Meter Replacement Surcharge in Case No 2019-00131.¹⁶ It subsequently replaced meters and made other small capital investments with surcharge proceeds.¹⁷ Collection of the surcharge was discontinued in January 2025.¹⁸ Southern District requested a Water Loss Reduction Surcharge of \$6.83 per

¹⁵ See generally Commission Final Orders for Rate Applications from 2017-present for language explaining the greater emphasis on encouraging efforts to reduce water loss and including the approximate amount of money the lost water represented to the utility. Case No. 2017-00176, *Electronic Application of Estill County Water District No. 1 for Rate Adjustment Pursuant to 807 KAR 5:076* (Ky. PSC Dec. 20, 2017), Order at 4

¹⁶ Case 2019-00131 *Application of Southern Water and Sewer District for an Alternative Rate Adjustment* (Ky. PSC Nov. 7, 2019), Order at 13, ordering paragraph 4.

¹⁷ Case 2020-00121, *Electronic Southern Water & Sewer District Meter Replacement Surcharge Monitoring* (Ky. PSC Jan 31, 2024) Order, (Ky. PSC Aug 4, 2023) Order, and (Ky. PSC Mar 17, 2021) Order.

¹⁸ Southern District's Response to Staff's Second Request, Item 2, 2_Board_Minutes_2025, at 2, January 27, 2024, meeting, Item D.

customer per month in this case.¹⁹ This proposed charge will be discussed in the Summary of Recommendations below.

DISCUSSION

Using its pro forma test-year operations, Southern District's application determined that a base rate revenue increase of \$489,325, or 15.23 percent, was necessary to achieve the revenue requirement as shown in the table below.²⁰ However, in Southern District's Response to Staff's Second Request, it submitted a modified rate study including a corrected billing analysis which reflected a revised proposed revenue increase to \$185,529, or 5.28 percent.²¹ Since Southern District did not amend its application, the adjustments based on the corrected billing analysis are incorporated into Commission Staff's adjustments rather than in Southern District's proposed adjustments in the Pro Forma Operating Statement later in this document.

¹⁹ Remediated ARF Application, ARF-Application_2023_Test_Year.pdf, (filed Dec. 26, 2024), Attachment 1, Customer Notice, at 8.

²⁰ Cover letter and Alternative Rate Filing application, ARF_Application_2023_Test_Year.pdf, Attachment 4, Revenue Requirements Table.

²¹ Southern District's Response to Staff's Second Request, Item 3, 3_Rate_Study_TY_2023_with_Corrected_Billing Analysis.

Description	Southern Water District Application
Pro Forma Operating Expenses	\$ 3,532,554
Average Annual Principal and Interest Payments	261,384
Additional Working Capital at 20%	52,277
Total Revenue Requirement	3,846,215
Other Revenue and Non Utility Income ()	(137,423)
Interest Income ()	(6,540)
Revenue Required From Water Sales	3,702,252
Revenue from Sales at Present Rates ()	(3,212,927)
Required Revenue Increase / (Decrease)	\$ 489,325
Percentage Increase / (Decrease)	15.23%

To determine the reasonableness of the rates requested by Southern District, Commission Staff performed a limited review of Southern 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 measurable²² 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.

²² 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); and 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 recommendations are summarized in this report. Jeff Abshire reviewed the calculation of Southern District's Overall Revenue Requirement, and Jason Green reviewed Southern District's reported revenues and rate design.

SUMMARY OF RECOMMENDATIONS

Overall Revenue Requirement and Required Revenue Increase. By applying the Operating Ratio (OR) method, as generally accepted by the Commission, Commission Staff determined that Southern District's revenue required from water sales is \$4,063,069 to meet the Overall Revenue Requirement of \$4,206,136 and that a \$765,782 revenue increase, or 23.22 percent, to pro forma present rate revenues is necessary to generate the Overall Revenue Requirement.

Monthly Water Service Rates. Southern District proposed to increase its monthly retail water service rates by approximately 15.23 percent across the board based on the amount requested in its application.²³ Southern District's response to Staff's Second Request included a correction for an error in its application which reduced the proposed percentage increase to 5.28 percent.²⁴ Southern District has not performed a cost of service study (COSS). Southern District stated that it did not complete a COSS at this time as there have been no material changes in the water system.²⁵

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

²³ Application, ARF_Application_2023_Test_Year.pdf, Attachment 1, Customer Notice.

²⁴ Southern District's Response to Staff's Second Request, Items, Item 10b; Item 3, 3_Rate_Study_TY_2023_with_Corrected_Billing Analysis, SAO Tab, Revenue Requirements table.

²⁵ Southern District's Response to Staff's First Request, Item 22.

the absence of a COSS.²⁶ Finding no such evidence in this case, Commission Staff followed the method previously accepted by the Commission and allocated the \$765,782 revenue increase evenly across the board to Southern District's monthly retail water service rates.

The rates, which are set forth in Appendix B 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 \$4,063,069 Revenue Required from Rates. The rates will increase a typical residential customer's monthly base rate water bill from \$54.55 to \$67.22, an increase of \$12.67, or approximately 23.23 percent.²⁷ Including the effects of the elimination of the Water Meter Replacement Surcharge of \$5.25 per customer per month and the addition of the water loss surcharge of \$6.83 per customer per month would result in an increase to the average bill of \$68.80, an increase of \$14.25, or approximately 26.12 percent. A comparison of the rates is shown in the table below.

Description	Notes	Tariff (08/22/2023)	Southern District Application Notice	Commission Staff Calculation
Base Rate (4,000 gallons)		\$ 54.55	\$ 62.86	\$ 67.22
Meter Replacement Surcharge	(1)	5.25	5.25	0.00
Water Loss Reduction Surcharge		0.00	6.83	6.83
Total Cost Per Customer Per Month		<u>\$ 59.80</u>	<u>\$ 74.94</u>	<u>\$ 74.05</u>
Base Rate Increase v. Tariff			15.23%	23.23%
Base Rate Increase (Commission Staff) v. Application				6.94%
Total v. Tariff			25.32%	23.83%
Total (Commission Staff) v. Application				-1.19%

(1) Meter Replacement Surcharge billing was discontinued January 2025 but remains in the tariff.

²⁶ Case No. 2021-00218, *Electronic Application of Madison County Utilities District for an Alternative Rate Adjustment* (Ky. PSC Jan. 5, 2022).

²⁷ Application, ARF_Application_2023_Test_Year.pdf, Attachment 1, Customer Notice.

Nonrecurring Charges. Southern District provided updated cost justification information for the Non-Recurring Charges.²⁸ The Commission has previously found that because district personnel are paid during regular business hours, estimated additional regular business hour labor costs previously included in determining the amount of Non-Recurring Charges should be eliminated.²⁹ These costs were removed from Southern District's nonrecurring charges in Case No. 2022-00099.³⁰ The cost justification information shown in Appendix A, reflects cost updates to those amounts since the labor costs were removed. Commission Staff could not determine where Southern District reported nonrecurring charge revenue in its Schedule of Adjusted Operations (SAO) during the test year. Southern District stated that there was an issue with the software in 2023 that didn't group non-recurring charges.³¹ Commission Staff calculated that Southern District should have recovered \$26,910 in nonrecurring charges during the test year based upon the occurrences provided and the current charges. The table below reflects the revisions to nonrecurring charges as well as the components of the pro forma nonrecurring charge revenue of \$18,885, which is reported in pro forma Miscellaneous Service Revenues in the SAO. Commission Staff recommends that the Commission

²⁸ Southern District's Amended Response to Staff's First Request, Item 27, 27_Nonrecurring_Charges_Cost_Justifications.pdf.

²⁹ Case No. 2023-00299, *Electronic Application of Magoffin County Water District for a Rate Adjustment Pursuant to 807 KAR 5:076* (Ky. PSC May 24, 2024); Case No. 2023-00284, *Electronic Application of Montgomery County Water District No. 1 for a Rate Adjustment Pursuant to 807 KAR 5:076* (Ky. PSC Mar. 5, 2024); Case No. 2023-00258, *Electronic Application of Kirksville Water Association, Inc. for a Rate Adjustment Pursuant to 807 KAR 5:076* (Ky. PSC May 3, 2024); and Case No. 2023-00220, *Electronic Application of East Casey County Water District for a Rate Adjustment Pursuant to 807 KAR 5:076* (Ky. PSC May 21, 2024).

³⁰ Case 2022-00099 (Ky. PSC, Dec. 20, 2022), at 10–11, ordering paragraph 4 and Appendix A.

³¹ Southern District's Supplemental Response to Staff's Second Request, Item 13a.

accept Southern District's proposed adjustments for the charges mentioned above, as Southern District supported these with the cost justification provided,³² and the amounts meet the ratemaking criteria of being known and measurable. The cost justification information, also shown in Appendix A, was provided by Southern District and supports Commission Staff's adjustments to the Nonrecurring Charges.

Description	Occurrences	Current Charge	Revised Charge	Adjustment	Pro Forma
Connection/Turn-On Charge	806	\$20.00	\$11.00	(7,254)	\$ 8,866
Connection/Turn-On Charge (After Hours)	0	\$88.00	\$84.00	0	0
Meter Relocation Charge	2	Actual Cost	Actual Cost	0	560
Meter Re-Read Charge	0	\$20.00	\$11.00	0	0
Meter Test Charge	0	\$50.00	\$81.00	0	0
Reconnection Charge	480	\$20.00	\$11.00	(4,320)	5,280
Reconnection Charge (After Hours)	0	\$88.00	\$99.00	0	0
Returned Check Charge	63	\$10.00	\$15.00	315	945
Service Call/Investigation	0	\$20.00	\$11.00	0	0
Service Call/Investigation (After Hours)	0	\$88.00	\$84.00	0	0
Disconnection Charge (New Charge)	294	\$0.00	\$11.00	3,234	3,234
Pro Forma					18,885
Test Year					26,910
Adjustment					<u>\$ (8,025)</u>

In response to Staff's First Request, Southern District indicated there were 294 instances of a "disconnect charge" with revenues totaling \$5,880 from this charge.³³

³² Southern District's Amended Response to Staff's First Request, Item 27, Nonrecurring Charge Cost Justifications.

³³ Southern District's Response to Staff's First Request, Item 26.

However, the disconnection charge is not in the current tariff,³⁴ nor is it included in its notice.³⁵ In its response to Staff's Second Request, Southern District stated that the disconnection charge is a new charge and provided cost justification for the charge.³⁶ Commission Staff inquired as to how this could be a new charge if the charge is already being assessed to customers. In response to Staff's Third Request, Southern District clarified that the disconnection charge was first assessed on October 4, 2022, but stated that there is no tariff or case number where the Commission approved the charge.³⁷ Commission Staff recommends that the Commission accept Southern District's proposed disconnection charge of \$11.00 as the cost justification provided supports this amount.

Commission Staff notes that KRS 278.160(2) states that "no utility shall charge, demand, collect, or receive from any person a greater or less compensation for any service rendered or to be rendered than that prescribed in its filed schedules, and no person shall receive any service from any utility for a compensation greater or less than that prescribed in such schedules." Therefore, Commission Staff recommends that the Commission open an investigation to address Southern District's assessment of an unapproved rate since approximately October 2022.

In addition to its nonrecurring charges, Southern District provided updated cost justification sheets for its Meter Tap-On Fees for its 3/4-inch meters, 1-inch meters, and proposed a new Tap-On Fee for 2-inch meters. The updated cost justification sheets

³⁴ P.S.C. Ky. 1, 2nd Revised Sheet No. 5 (issued Jan. 20, 2023), effective Dec. 20, 2022.

³⁵ Cover letter and Alternative Rate Filing application, ARF_Application_2023_Test_Year.pdf, Attachment 1, Customer Notice.

³⁶ Southern District's Response to Staff's Second Request, Item 13c.

³⁷ Southern District's Response to Staff's Third Request, Item 13.

support a tap-on fee of \$1,548 for its 3/4-inch meters, an increase from the current fee of \$750, \$1,885 for its 1-inch meters, an increase from the current fee of \$850, and \$5,500 for its 2-inch meters. Commission Staff reviewed the cost justification sheets³⁸ provided by Southern District and recommends an increase in its Meter Tap-On Fee for 3/4-inch meter sizes, 1-inch meter sizes, and the new charge for 2-inch meter sizes, as the revised cost justification supports a higher cost.

Water Meter Replacement Surcharge. Southern District was authorized in Case No. 2019-00131 to collect a meter replacement surcharge of \$5.25 per customer per month for 60 months or until the cost of new meters had been collected, whichever occurred first.³⁹ The purpose of the surcharge was to fund and replace all of Southern District's customer meters. A separate monitoring case was established, Case No. 2020-00121, to facilitate Commission oversight of surcharge collections and spending.⁴⁰ Southern District discontinued billing of the surcharge in January 2025.⁴¹

Water Loss Surcharge. In its application, Southern District proposed a water loss surcharge of \$6.83 per customer per month "to help lower system losses to more acceptable levels".⁴² It stated that the term of the surcharge would be 5 years, and it

³⁸ Southern District's Response to Staff's First Request, Item 27.

³⁹ Case No. 2019-00131, (Ky. PSC Nov 7, 2019), Appendix.

⁴⁰ Case No. 2020-00121 Electronic Southern Water & Sewer District Meter Replacement Surcharge Monitoring (Ky. PSC Apr 8, 2020).

⁴¹ Southern District's Response to Staff's Second Request, Item 2, 2_Board_Minutes_2025, Regular Scheduled Meeting January 27, 2025, Item D. Southern District's Amended Response to Staff's First Request, Item 28.

⁴² Remediated ARF Application, ARF-Application_2023_Test_Year.pdf, (filed Dec. 26, 2024), Attachment 1, Customer Notice, at 8; Attachment 2, Reasons for Application, at 10.

would generate \$441,846.36 per year, or \$2,209,231.80 in total.⁴³ Southern District proposed to add a “third crew”, a complement of small capital items totaling \$230,000, and mostly replacement of various service lines with the surcharge funds.⁴⁴ The two-person crew would be tasked with water loss reduction efforts including replacing service lines in multiple areas. Southern District noted that the Wayland to Lackey project “was cut down due to budget issues, leaving out all the service lines in that area.” The end result is that Southern District has new main lines and what it referred to as a sprinkler system attached to all the new main lines.⁴⁵ Southern District stated

[t]he Projects are endless due to the past management. It will take several years to straighten all these mishaps from the past. There are several areas we know that has thefts and the only way we can see all of them is to relay sections of line. We have more projects than can be completed in 10 years with two crews.⁴⁶

Southern District’s water loss issues are well established in Case No. 2019-00131⁴⁷ and Case No. 2020-00121,⁴⁸ as well as in its Annual Report filings with the Commission.⁴⁹ The amount of water loss in excess of 15 percent that cannot be recovered for ratemaking purposes in this case approximates \$445,000 as described in

⁴³ Southern District’s Response to Staff’s Third Request, Item 20a.

⁴⁴ Southern District’s Response to Staff’s Third Request, Item 20b.

⁴⁵ Southern District’s Response to Staff’s Third Request, Item 20b.

⁴⁶ Southern District’s Response to Staff’s Third Request, Item 20b.

⁴⁷ Case No. 2019-00131, Nov. 7, 2019 Order at 4–5.

⁴⁸ Case No. 2020-00121, *Electronic Southern Water & Sewer District Meter Replacement Surcharge Monitoring*.

⁴⁹ *Annual Report of Southern Water and Sewer District, Inc. to the Public Service Commission for the Calendar Year Ended December 31, 2021* (2021 Annual Report) at 57. *Annual Report of Southern Water and Sewer District, Inc. to the Public Service Commission for the Calendar Year Ended December 31, 2022* (2022 Annual Report) at 57. 2023 Annual Report at 57.

Item I, Excess Water Loss, discussed later in this report. Commission Staff also cannot conclude the extent to which Southern District's current staffing costs are directly related to excess water loss. Commission Staff also could not determine if significant activities for line replacements have historically, and are currently, occurring that should have been capitalized during that year. Those costs should have instead been recovered in rates via depreciation expense over the depreciation life of each project.

The cost of water loss in excess of 15 percent that is disallowed for ratemaking purposes as well as the cost of labor to both repair and attempt to complete small projects (that are expensed) represents an ongoing drain on Southern District's cash flow. Had Southern District sought additional funding to address the "budget issues" noted for the Wayland to Lackey project, it would not be facing a longer-term fix that it now proposes to complete the project on its own. Commission Staff recommends that Southern District develop a capital plan specifically addressing water loss reduction. This plan should include financing alternatives to fund the projects identified in the plan using base rates to support low interest loans rather than continue to fund its water loss reduction efforts through additional staff and indirect capital investments using surcharges. Southern District's initial capital projects should include the completion of all service line replacement projects that its current and proposed additional staff are intended to address.

Commission Staff recommends that the Commission approve Southern District's request for a water loss surcharge of \$6.83 per customer per month for a period of up to 60 months. Commission Staff further recommends that the Commission establish a separate proceeding to monitor the surcharge and place strict controls over the use of the

funds. Specifically, Commission Staff recommends limiting the use of the funds to 1) an overall infrastructure evaluation including preparation of a professionally developed 15-to-20-year capital plan that prioritizes water loss initiatives, and 2) partial funding of the capital plan, including first year debt service for the highest priority projects. Commission Staff recommends that Southern District be required to retain a professional engineering firm, solicited through a competitive request for qualifications and proposals process. Commission staff notes that the Kentucky Rural Water Association and many of the Area Development Districts can assist Southern District in that solicitation process. The overall infrastructure plan should identify and prioritize projects to significantly impact the water loss amounts. Commission Staff recommends that the surcharge be terminated once the plan is developed, and initial projects are funded and incorporated into Southern District's base rates.

PRO FORMA OPERATING STATEMENT

Southern District's Pro Forma Operating Statement for the test year ended December 31, 2023, as determined by Commission Staff, is presented in the table below.

Description	Test Year	Southern Water District Application Adjustments	Commission Staff Adjustments	Total Adjustments	(Ref)	Pro Forma
Operating Revenues						
Metered Retail Sales	\$ 3,262,150	\$ (158,990)	\$ 303,894	\$ 144,904	(A1)	
			(211,269)	(211,269)	(A2)	3,195,785
Sales for Resale	109,767		(8,265)	(8,265)	(A3)	101,502
Forfeited Discounts	89,107			0		89,107
Miscellaneous Service Revenues	33,943		(15,058)	(15,058)	(B)	18,885
Total Operating Revenues	3,494,967	(158,990)	69,302	(89,688)		3,405,279
Operation and Maintenance						
Salaries and Wages - Employees	739,852		45,304	45,304	(C1)	
			111,277	111,277	(C2)	
			(4,950)	(4,950)	(D1)	891,483
Salaries and Wages - Officers	18,000		(18,000)	(18,000)	(E)	0
Employee Benefits - Medical	201,573		58,809	58,809	(F1)	
			(67,945)	(67,945)	(F2)	192,437
Purchased Water	401,919	(167,559)	4,204	(163,355)	(H1)	
			(5,732)	(5,732)	(G1)	
			(4,352)	(4,352)	(G2)	228,480
Purchased Power	406,768	(169,580)	(2,390)	(171,970)	(I)	
			5,732	5,732	(G1)	240,530
Chemicals	263,427	(109,822)		(109,822)	(H)	153,605
Materials and Supplies	274,202		(11,550)	(11,550)	(D2)	262,652
Contractual Services (5 items)	393,494			0		393,494
Rents	8,428			0		8,428
Transportation Expenses	106,424			0		106,424
Insurance (3 items)	100,342			0		100,342
Advertising Expense	5,645			0		5,645
Bad Debt	1,142,457	(989,985)	(56,244)	(1,046,229)	(J)	96,228
Miscellaneous	25,595			0		25,595
Total	4,088,126	(1,436,946)	54,163	(1,382,783)		2,705,343
Amortization	2,460			0		2,460
Depreciation Expense	864,145	(45,586)		(45,586)	(K)	
			388	388	(D3)	
			38,934	38,934	(K1)	857,881
Taxes Other Than Income	60,354		11,978	11,978	(L)	72,332
Total Operating Expenses	5,015,085	(1,482,532)	105,463	(1,377,069)		3,638,016
Net Operating Income	(1,520,118)	1,323,542	(36,161)	1,287,381		(232,737)
Interest Income	0		6,540	6,540	(M)	6,540
Nonutility Income - Third Party Billing / Collections	0		14,373	14,373	(N1)	
			14,162	14,162	(N2)	28,535
Income Available to Service Debt	\$ (1,520,118)	\$ 1,323,542	\$ (1,086)	\$ 1,322,456		\$ (197,662)

(A) Metered Revenues. In its application, Southern District proposed an adjustment to decrease Metered Retail Sales by \$158,990. In its response to Staff's

Second Request, Southern District submitted a revised billing analysis and revised SAO and proposed an adjustment to increase Metered Retail Sales by \$144,904 (A1).⁵⁰ Commission Staff reviewed Southern District's revised billing analysis and disagrees with its adjustment because Southern District did not use the correct sales amount of \$3,262,150 that is reported in its 2023 Annual Report. Commission Staff made an adjustment to decrease Metered Retail Sales by \$211,269 (A2) to reflect the correct pro forma Metered Retail Sales of \$3,195,785. The net effect of Southern District and Commission Staff adjustments is to reduce Metered Retail Sales by \$66,365. Commission Staff recommends that the Commission accept the adjustment because the amount meets the ratemaking criteria of being known and measurable.

In addition to a revision to its metered retail water sales, Southern District also proposed an adjustment to its revenue from sales for resale. Its revised billing analysis reflects revenue from sales for resale of \$101,502. This results in a decrease of \$8,265 to test year sales for resale. Commission Staff recommends that the Commission accept the adjustment because the amount meets the ratemaking criteria of being known and measurable.

(B) Miscellaneous Service Revenues. Southern District reported Miscellaneous Service Revenues of \$33,943. Commission Staff reviewed the 2023 general ledger and made three adjustments. First, Commission Staff removed \$2,071 (B1) in tap fees that were recorded in account number 47103, Tap Fees, which should

⁵⁰ Southern District's Response to Staff's Second Request, Item 10b, 3_Rate_Study_TY_2023_with_Corrected_Billing_Analysis.xlsx.

have been recorded as contributed capital.⁵¹ Second, Commission Staff removed \$31,872 (B2) for an insurance reimbursement that will not recur.⁵² Third, Commission Staff added \$18,885 (B3) for nonrecurring charges that were not properly classified in the general ledger as discussed earlier in this Report. The adjustments, which net to a decrease of \$15,058, are shown in the table below. Commission Staff recommends that the Commission accept the total adjustment because the amount meets the ratemaking criteria of being known and measurable.

Description	Test Year	Utility Adjustments	Commission Staff Adjustments	Pro Forma	Ref
Tap Fees	\$ 2,071	\$ -	\$ (2,071)	\$ -	(B1)
Other Income	31,872	0	(31,872)	0	(B2)
Non-Recurring Charges	0	0	18,885	18,885	(B3)
Total	<u>\$ 33,943</u>	<u>\$ -</u>	<u>\$ (15,058)</u>	<u>\$ 18,885</u>	

(C) Salaries and Wages - Employees. Southern District did not propose any adjustments to salaries and wages. Commission Staff reviewed 2023 and 2024 wages and hours⁵³ and noted that the 2024 amounts were higher than 2023. Southern District stated that 2024 is indicative of recurring operations⁵⁴ and that its full staffing is 25 full-time and 0 part-time employees.⁵⁵ Commission Staff made two adjustments. First, Commission Staff increased wages by \$45,304 (C1) to reflect 2024 wage rates, hours

⁵¹ Southern District's Response to Staff's First Request, Item 1a, 1a_General_Ledger_2023.xlsx, account 471003 Tap Fees.

⁵² Southern District's Response to Staff's Second Request, Item 11b.

⁵³ Southern District's Amended Responses to Staff's First Request, Item 4, 4_Employee_Earnings_2023.xlsx; also 4_Employee_Earnings_2024.xlsx.

⁵⁴ Southern District's Supplemental Response to Staff's Second Request, Item 6.

⁵⁵ Southern District's Response to Staff's Second Request, Item 5.

and changes in employee turnover compared to the test year.⁵⁶ Second, Commission Staff increased wages by \$111,277 (C2) based on average 2024 pay rates, to normalize straight time hours to reflect 25 full-time positions at 2,080 annual hours each. A walk forward of test year wages to calculated pro forma wages is shown in the *Wage Adjustments* table below. The *Average 2024 Straight Time Wage Rate* table below provides details on how the average hourly rate was derived. Commission Staff notes that Southern District's board voted in December 2023 to cease annual merit raises until resolution of the rate case.⁵⁷ Southern District stated that its "board anticipates reinstating general wage increases as soon as funding is made available. Southern District is aware that it is not able to compete with many other employers on the basis of salary/pay alone but Southern must keep their rates of pay reasonable in order to attract and retain quality employees."⁵⁸ Since Southern District's board did not commit to an increase for 2025, Commission Staff is unable to include an adjustment to reflect a salary increase in the pro forma. Commission Staff recommends the Commission accept the Commission Staff's adjustments because the amount meets the ratemaking criteria of being known and measurable.

⁵⁶ Southern District's Amended Response to Staff's First Request, Item 4, 4_Employee_Earnings_2024.xlsx.

⁵⁷ Southern District's Response to Staff's First Request, Item 10, 10_Board_Minutes_2023.pdf, at 29, Item I.

⁵⁸ Southern District's Response to Staff's Second Request, Item 8c.

Wage Adjustments

Description	Amount	Ref
Test Year Wages	\$ 739,852	
Adjust to 2024 Hours / Wage Rate Mix	45,304	C1
Normalize Wages to 25 Employees at 2,080 Hours Each at Average Straight Time Rate	111,277	C2
Total Wages	896,433	
Capitalize Tap Fee Labor	(4,950)	D1
Pro Forma Wages	<u>\$ 891,483</u>	

Average 2024 Straight Time Wage Rate

Straight Time Categories	2024 Hours	2024 Wages
Wages	42,857.46	\$ 663,283.41
Sick	16.00	263.36
Holiday	1,840.00	28,318.49
Personal	96.00	1,583.47
Total 2024 Actual	44,809.46	693,448.73
Adjust Hours for 25 Full Time Employees at Average Wage Rate at 2,080 Hours Each	7,190.54	111,277.00
Pro Forma	<u>52,000.00</u>	<u>\$ 804,725.73</u>

Average Straight Time Rate (2024 Wages
Divided by 2024 Hours)

\$ 15.48

(D) Costs Related to Meter Installation. During the test year, Southern District reported \$2,071 in Tap On Fees.⁵⁹ The Uniform System of Accounts for Class A/B Water Systems (USoA) requires that these costs be capitalized as Utility Plant in Service and depreciated over their estimated useful lives.⁶⁰ During the test year, Southern District

⁵⁹ Southern District's Response to Staff's First Request, Item 1b, 1b_Trial_Balance_2023.xlsx, Account 47103 Tap fees.

⁶⁰ USoA, Accounting Instruction 19 and 33.

installed 22 new water connections.⁶¹ Using the current tariff rate of \$750 per connection, Commission Staff calculated \$16,500 of Tap Fee expenditures, the cost of which was not capitalized.⁶² Commission Staff calculated a decrease of \$4,950 (D1) to Salaries and Wages – Employees Expense and a decrease of \$11,550 (D2) to Materials and Supplies as shown in the table below. Commission Staff also increased depreciation expense by \$388 (D3).

Description	Percent	Dollars	Ref
Salaries and Wages	30.0%	\$ 4,950	(D1)
Materials	70.0%	11,550	(D2)
Total		<u>\$ 16,500</u>	
NARUC Service Life / Depreciation	42.50	<u>\$ 388</u>	(D3)

Commission Staff recommends the Commission accept Commission Staff's proposed adjustments to decrease Salaries and Wages – Employees by \$4,950 and decrease Materials and Supplies by \$8,085 because it reflects the proper accounting for water connection expenses according to the USoA.

(E) Salaries and Wages – Officers. Southern District has 5 commissioners who are each paid \$6,000 per year.⁶³ It reported \$18,000 in test year wages and did not propose any adjustments. Commission Staff verified appointments by the Floyd County

⁶¹ Southern District's Amended Response to Staff's First Request, Item 20a.

⁶² Southern District's Amended Response to Staff's First Request, Item 20b and Item 20c.

⁶³ Southern District's Response to Staff's First Request, item 11, 11_Commissioners.pdf.

Fiscal Court⁶⁴ as well as training records.⁶⁵ However, Commission Staff could not verify proper pay authorization. Southern District stated “[t]here are no fiscal court minutes showing authorization for the board members to receive compensation. That was done here by Former Management.”⁶⁶ Southern District also provided an email exchange with a Floyd County Fiscal Court representative which stated, in part, “[t]he biggest challenge I see is that Judge Williams didn't think we would have had such a resolution because the Fiscal Court does not control what the water company does. He thought it was Southern Water's decision to provide that compensation. It is no different than any other water company.”⁶⁷ KRS 74.020(6) states that “[e]ach commissioner shall receive an annual salary of not more than thirty-six hundred dollars (\$3,600)” and that

[A]ny such amount the salary shall be fixed by the county judges/executive with the approval of the fiscal court; in multicounty districts, it shall be fixed by the agreement between the county judges/executive with the approval of their fiscal courts. In fixing and approving the salary of the commissioners, the county judge/executive and the fiscal court shall take into consideration the financial condition of the district and its ability to meet its obligations as they mature.

Commission Staff reduced pro forma officer salaries by the \$18,000 test year amount because Southern District's officer compensation was not properly authorized by the fiscal court as required by KRS 74.020(6). Commission Staff recommends that Southern District request the Floyd County Fiscal Court to update its authorization of

⁶⁴ Southern Districts Response to Staff's First Request, Item 11a, 11a_Fiscal_Court.pdf; Southern Districts Response to Staff's Second Request, Item 3, 3_Fiscal_Court_Minutes.pdf.

⁶⁵ Southern Districts Response to Staff's First Request, Item 11b, 11b_Commissioner_Training.pdf.

⁶⁶ Southern District's Response to Staff's Third Request, Item 19.

⁶⁷ Southern District's Response to Staff's Third Request, item 19, 19_Commissioner_Compensation.pdf.

Southern District Commissioner compensation amounts as soon as possible. Commission Staff further recommends that Southern District request the Floyd County Fiscal Court to include Southern District Commissioner compensation authorization in Fiscal Court minutes upon the appointment or reappointment of each future Southern District commissioner.

Commission Staff recommends that the Commission deny recovery of Southern District's commissioner compensation due to the absence of authorization by the Floyd County Fiscal Court.

(F) Employee Benefits. Southern District did not propose any adjustments to employee benefits. Commission Staff made two adjustments which result in a net decrease of \$9,136 (F1 and F2) as described below. Southern District provides dental, vision, life, and medical insurance to its employees. Employee contributions are required in varying amounts, depending on coverage classification, for medical insurance coverage.⁶⁸ Southern District also facilitates various supplemental insurance coverages where it pays the invoices, but employees pay 100 percent of the premium.⁶⁹ A 401k plan is available to each employee that matches half of employee contributions up to 3 percent.⁷⁰

The Commission continues to place greater emphasis on evaluating employees' total compensation packages, including benefit programs, for market and geographic competitiveness to ensure the development of a fair, just, and reasonable rate. The

⁶⁸ Southern District's Response to Staff's Third Request, Item 3.

⁶⁹ Southern District's Response to Staff's Second Request, Item 1a.

⁷⁰ Southern District's Response to Staff's Second Request, Item 1a.

Commission has found that, in most cases, 100 percent of employer-funded health care does not meet those criteria.⁷¹ Southern District stated its employees' contribution is based on coverage class, with Employee Only plans contributing \$25 biweekly, employee /spouse and employee/children contributing \$50 biweekly, and family plans requiring \$75 contributions biweekly.⁷² This results in average employee contribution of 5.89 percent to medical insurance.

Because Southern District's employee contribution is below the national average from the 2024 Bureau of Labor Statistics Study (BLS Study) on employee contributions,⁷³ and because Southern District did not provide sufficient evidence or comparative information in the record to support any variance from the averages contained in a nationally recognized survey, Commission Staff recommends an adjustment to the average employee contributions for private industry workers of 20 percent for single coverage and 32 percent for family coverage provided by the BLS Study. Southern District does not require employee contributions for dental insurance, which is lower than the recommended average employee contribution in the Willis Benchmarking Survey of 60 percent for the national average for an employee's contribution to dental insurance that is consistent with Commission precedent.⁷⁴

⁷¹ Case No. 2020-00167, *Electronic Application of Ohio County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 3, 2020); Case No. 2020-00296, *Electronic Application of Allen County Water District for an Alternative Rate Adjustment* (Ky. PSC Feb. 3, 2021).

⁷² Southern District's Response to Staff's Third Request, Item 3.

⁷³ U.S. Bureau of Labor Statistics, Share of Premiums Paid by Employer and Employee for Single Coverage, March 2023 <https://www.bls.gov/news.release/ebs2.t03.htm>, U.S. Bureau of Labor Statistics, Share of Premiums Paid by Employer and Employee for Family Coverage, March 2023 <https://www.bls.gov/news.release/ebs2.t04.htm>.

⁷⁴ See Case No. 2017-00263, *Electronic Application of Kentucky Frontier Gas, LLC for Alternative Rate Adjustment* (Ky. PSC Dec. 22, 2017), Order at 9-10; and The Willis Benchmarking Survey, 2015, at

Commission Staff made two adjustments for a net expense decrease of \$9,136 and a pro forma amount of \$192,437 (F). First, Commission Staff increased expense by \$58,809 to \$271,957 (F1) to reflect aggregate changes in the costs of insurance programs from the 2023 test year to 2025 costs.⁷⁵ The effect of employee turnover throughout the test year to 2025 is a component of this adjustment as well. Second, Commission Staff decreased expense by \$67,945 to (\$79,520) (F2) to reflect adjustments for employee contribution amounts based on the BLS Study and the Willis Benchmarking Survey. The adjustments described above result in a pro forma yearly benefit cost of \$192,437 as shown in the tables below. Commission Staff recommends the Commission accept the Commission Staff's adjustments because the amounts are known and measurable, are consistent with Commission precedent, and match the information provided in the case record.

Employee Benefits Summary

Benefit	Test Year	Adjustments	Pro Forma	Ref
Health	\$ 190,807	\$ 63,866	\$ 254,673	
Dental	7,062	814	7,876	
Life	9,099	(7,971)	1,128	
401K	6,180	2,100	8,280	
Net Cost Impact	213,148	58,809	271,957	(F1)
<i>Pro Forma Employee Contributions</i>				
BLS Adjustment	(11,575)	(61,497)	(73,072)	
Dental, Vision, Life Adjustmen	na	(6,448)	(6,448)	
Net	(11,575)	(67,945)	(79,520)	(F2)
Total	\$ 201,573	\$ (9,136)	\$ 192,437	(F)

62-63. (https://www.willis.com/Documents/publications/Services/Employee_Benefits/20151230_2015WillisBenefitsBenchmarkingSurveyReport.pdf).

⁷⁵ Southern District's Response to Staff's Third Request, Item 2b, KLG_Health_Trust_2025; Item 2c, Dental_and_Vision_2025; Item 2c, Dental_and_Vision_2025

Employee Benefits Calculations

Type of Premium	Number of Employees	Sample 2025 Premium	Monthly Employee W/H \$	Employee W/H %	Total Annual Premium	Annual Employee W/H	Net Cost	Employee Contribution BLS %	Calculated Employee W/H
<i>Medical Coverage</i>									
Employee (EMP)	7	\$ 835.54	50.00	5.98%	\$ 70,185	\$ (4,200)	\$ 65,985	20%	\$ 14,037
Employee / Child or Children (E)	2	1,503.97	100.00	6.65%	36,095	(2,400)	33,695	32%	11,550
Employee / Spouse (ESP)	4	1,754.64	100.00	5.70%	84,223	(4,800)	79,423	32%	26,951
Family (FAM)	2	2,673.72	150.00	5.61%	64,169	(3,600)	60,569	32%	20,534
Total Participants	15			5.89%	254,673	(15,000)	239,673	29%	73,072
BLS Adjustment						(58,072)	(58,072)		(15,000)
Net Medical Insurance					\$ 254,673	\$ (73,072)	\$ 181,601		\$ 58,072
<i>Other Benefits</i>									
Delta Dental (Dental)		532.42	0.00	0%	6,389	0	6,389	60%	3,833
Delta Dental (Vision)		123.92	0.00	0%	1,487	0	1,487	100%	1,487
Life		94.03	0.00	0%	1,128	0	1,128	100%	1,128
401K (used 2024)		690.00	0.00	0%	8,280	0	8,280	-	0
Sub-total Other Benefits					17,284	0	17,284		6,448
Net Adjustment to Pro Forma Employee Contribution						(6,448)	(6,448)		
Net Other Benefits					17,284	(6,448)	10,836		6,448
Total					\$ 271,957	\$ (79,520)	\$ 192,437		\$ 64,520

(G) Purchased Water. Southern District did not propose any adjustments to the cost of purchased water. Commission Staff reviewed the information submitted and made two adjustments as shown in the table below. The first adjustment is to reclassify \$5,732 (G1) from Purchased Water (decrease) to Purchased Power (increase) for an AEP invoice that was erroneously posted to general ledger account 60002, Water Purchases.⁷⁶ The second adjustment decreased the cost by \$4,352 (G2) to adjust the general ledger to the purchase quantities provided at the current cost.

⁷⁶ Southern District's Response to Staff's First Request, Item 1a, 1a_General_Ledger_2023.xlsx, Account 60002 Purchased Water, row 11,620.

Description	Knott County Water District	Pikeville	Prestonsburg	Total	Ref
Gallons	7,290,100	160,369,000	1,823,500	169,482,600	
Current Purchase Rate	\$ 3.2700	\$ 2.2600	\$ 3.050	\$ 2.3119	
Pro Forma Cost	<u>\$ 23,839</u>	<u>\$ 362,434</u>	<u>\$ 5,562</u>	<u>\$ 391,835</u>	
Test Year Purchase Cost				(401,919)	
Decrease in Purchase Cost				<u>\$ (10,084)</u>	(G)
<i>Adjustments</i>					
Reclass AEP to Purchased Power				\$ (5,732)	(G1)
Adjustment				(4,352)	(G2)
Total				<u>\$ (10,084)</u>	

Commission Staff recommends the Commission accept Commission Staff's adjustments to decrease Purchase Water Expense and to increase Purchased Power Expense by \$5,732 to ensure that expenses are recorded in the proper accounts.

(H) Purchased Power. Southern District did not propose any adjustments to Purchased Power expense. Commission Staff made one adjustment to increase the expense by \$5,732 for the reclassification adjustment described under Item (G1), Purchased Water, above. Commission Staff recommends the Commission accept Commission Staff's adjustment to Purchased Power because it records the expense in the proper account.

(I) Excess Water Loss. In its application, Southern District proposed adjustments to decrease Purchased Water Expense by \$167,559, Purchased Power Expense by \$169,580 and Chemicals Expense by \$109,822⁷⁷ to reflect the disallowance of water loss expenses in excess of 15 percent. During the test year, Southern District

⁷⁷ Remediated Application, ARF_Application_2023_Test_Year.pdf, Attachment 4, Schedule of Adjusted Operations, Adjustment B.

reported water loss of 56.6897 percent.⁷⁸ Commission regulations state that for ratemaking purposes, expenses for water loss in excess of 15 percent shall not be included for ratemaking purposes.⁷⁹ Commission Staff agrees with Southern District's methodology, however, the disallowed amounts changed as a result of the cost adjustments described in Purchased Water (G) and Purchased Power (H). First, disallowed Purchased Water Expense decreased by \$4,204 (H1) as a result of the \$10,084 (G1, G2) cost adjustment decreases. Second, disallowed Purchased Power Expense increased by \$2,390 (H2) as a result of the \$5,732 (G1) cost adjustment increase.

Total Water Loss

Description	Purchased Water	Purchased Power	Purchased Chemicals	Total
Pro Forma Purchases	\$ 391,835	\$ 412,500	\$ 263,427	\$ 1,067,762
Water Loss Percent	56.6897%	56.6897%	56.6897%	56.6897%
Total	<u>\$ 222,130</u>	<u>\$ 233,845</u>	<u>\$ 149,336</u>	<u>\$ 605,311</u>

Disallowed Water Loss

Description	Purchased Water	Purchased Power	Purchased Chemicals	Total
Pro Forma Purchases	\$ 391,835	\$ 412,500	\$ 263,427	\$ 1,067,762
Water Loss Percent in Excess of 15%	41.6897%	41.6897%	41.6897%	41.6897%
Total	<u>\$ 163,355</u>	<u>\$ 171,970</u>	<u>\$ 109,822</u>	<u>\$ 445,147</u>
Southern District Pro Forma Adjustments ()	<u>(167,559)</u>	<u>(169,580)</u>	<u>(109,822)</u>	<u>(446,961)</u>
Commission Staff (Decrease) / Increase to Southern District Proposed Adjustment	<u>\$ (4,204)</u>	<u>\$ 2,390</u>	<u>\$ -</u>	<u>\$ (1,814)</u>
	(H1)	(H2)		

Commission Staff recommends the Commission accept the adjustments to reduce pro forma expenses by \$445,147 for costs of water loss that are in excess of 15 percent because they reflect the application of 807 KAR 5:066, Section 6(3).

⁷⁸ 2023 Annual Water Report at 57.

⁷⁹ 807 KAR 5:066 (Water), Section 6(3) (Water Supply Measurement).

(J) Bad Debt Expense. Southern District proposed an adjustment to decrease Bad Debt Expense by \$989,985⁸⁰ to \$152,472⁸¹ to reflect a one-time nonrecurring entry to account for accumulation of account balances from prior years that have become uncollectible.⁸² Southern District stated that the amount was based upon the professional judgement of its accountant. Southern District stated that a written policy does not exist for when a balance is determined to be uncollectible, but that after individual account reviews and attempts to contact customers, an unpaid balance will be adjusted to bad debt expense after 90 days with no payment.⁸³ Commission Staff notes that Southern District reports gross accounts receivable in its general ledger at the functional level for Water (account number 14101), Garbage (account number 14102), Sewer (account number 14103), and Surcharge (account number 14109) billings. Southern District's provision for uncollectible accounts is reported in account number 14509 with no distinction of functional component.⁸⁴ Bad debts expense decreased from Southern District's adjusted test year amount of \$152,472⁸⁵ in 2023 to \$85,390 in 2024.⁸⁶ The provision for uncollectible accounts, a credit balance, decreased from (\$301,271.77) as

⁸⁰ Remediated Application, ARF_Application_2023_Test_Year.pdf, Attachment 4, Schedule of Adjusted Operations, Adjustment D.

⁸¹ Remediated Application, ARF_Application_2023_Test_Year.pdf, Attachment 4, Schedule of Adjusted Operations.

⁸² Remediated Application, ARF_Application_2023_Test_Year.pdf, Attachment 4, Schedule of Adjusted Operations, References, Adjustment D.

⁸³ Southern District's Response to Staff's Second Request, Item 17a.

⁸⁴ Southern District's Response to Staff's First Request, item 1a, 1a_General_Ledger_2023.xlsx.

⁸⁵ Remediated Application, ARF_Application_2023_Test_Year.pdf, Attachment 4, Schedule of Adjusted Operations.

⁸⁶ Southern District's Amended Responses to Staff's First Request, item 1a, S_1a_General_Ledger_2024.xls, account 76002 Bad Debt Expense.

of December 31, 2023, to (\$264,960.33) as of December 31, 2024. Southern District's write-off practices described above suggest that the amount applied to a reduction in the Provision for Uncollectible Accounts represents 2023 revenue that was written off in 2024 and that the reported \$85,390 bad debt expense in 2024 represents 2024 revenue that was written off during 2024. Based on Southern District's write-off practice statements and the general ledger activity for 2023 and 2024, Commission Staff concludes that Southern District likely reported an excess Provision for Uncollectible Accounts as of both December 31, 2023, and December 31, 2024, as its uncollectible reserve balance should not be greater than one fourth (approximately 90 days) of its asserted bad debt amount of \$152,472.

However, based on the information in the record, Commission Staff could not reach a conclusion about a reasonable level of current period uncollectible revenues. Given that the Commission recommends, in general, that utilities file for rate adjustments at least every three to five years,⁸⁷ Commission Staff recommends a pro forma amount for bad debts based on an average of the net of three years of Southern District's proposed pro forma bad debt expense of \$152,472 less the Provision for Uncollectible Accounts as of December 31, 2024, as shown in the table below. This results in an additional reduction of \$56,244 for a total pro forma reduction of \$1,046,229 as shown in the table below.

⁸⁷ Case No. 2024-00164, *Electronic Purchased Water Adjustment Filing of U. S. 60 Water District*, (Ky. PSC June 27, 2024). Case No. 2024-00154, *Electronic Purchased Water Adjustment Filing of West Shelby Water District* (Ky. PSC June 17, 2024).

Description	Amount
Dec 31, 2024 Provision for Uncollectible Accounts	\$ (264,960)
<i>Southern District's Pro Forma Bad Debt Expense</i>	
2025	152,472
2026	152,472
2027	152,472
Net Reserve Impact	\$ 192,456
Divisor (Years 2026, 2027)	2
Commission Staff Pro Forma	\$ 96,228
Southern District Pro Forma ()	(152,472)
Commission Staff Adjustment	(56,244)
Southern District Adjustment	(989,985)
Total Pro Forma Adjustment	<u>\$ (1,046,229)</u>

Commission Staff recommends that the Commission accept the pro forma adjustment to reduce bad debt expense by \$1,046,229 to reach a pro forma bad debt expense of \$96,228 because the method used to reach the pro forma expense reflects a reasonable methodology to use until Southern District's next recommend alternative rate filing. Commission Staff further recommends that the Commission recommend that Southern District improve its receivables management practices to reduce its losses from bad debts.

(K) Depreciation Expense. In its application, Southern District proposed an adjustment to decrease Depreciation Expense by \$45,586⁸⁸ to adjust depreciation lives to the midpoint of the recommended Average Service Life ranges from the NARUC

⁸⁸ Remediated Application, ARF_Application_2023_Test_Year.pdf, Attachment 4, Schedule of Adjusted Operations, Adjustment C.

publication titled “Depreciation Practices for small Utilities”.⁸⁹ Commission Staff reviewed Southern District’s proposed adjustment and agrees that it is reasonable.

However, Southern District did not propose any adjustments for assets placed in service subsequent to the test year. Commission Staff made two additional adjustments. First, Commission Staff increased depreciation by \$388 (D3) to reflect depreciation on tap fee costs described in the Costs Related to Meter Installations (item D) that were not capitalized by Southern District. Second, Commission Staff reviewed Southern District’s 2024 depreciation schedule⁹⁰ and identified fourteen assets with a cost of \$1,891,701.55 that were placed in service during 2024. Commission Staff calculated an additional \$38,934 (K1) in depreciation based on the NARUC depreciation lives for the assets as shown in the table below.

Asset No.	Description	Date	Cost	Book Life	2024 Deprec	NARUC Life Mid-point	Commission Staff Calculated Depreciation	NARUC Life Range	NARUC Acct Number
<i>Assets Placed in Service During 2024</i>									
453	Trailer - PJ Trailer	01/08/24	\$ 8,300.00	7.00	\$ 1,163.04	7.00	\$ 1,186	7	392
452	Transmission	01/18/24	4,754.84	7.00	647.71	7.00	679	7	392
449	Chevy Truck	02/20/24	28,500.00	7.00	3,515.22	7.00	4,071	7	392
451	Tablets PC	02/21/24	4,444.86	5.00	765.10	5.00	889	5	n/a
450	Hydrants 2	03/15/24	9,266.94	50.00	147.87	30.00	309	40 - 60	348
455	Wayland To Lackey Lines	04/01/24	1,463,413.90	50.00	21,991.19	62.50	23,415	50 - 75	343
445	Easement - S Ray Slone	04/16/24	907.07	0.00	0.00	0.00	0	0	n/a
446	Easement- Vernon K Slone	04/16/24	720.88	0.00	0.00	0.00	0	0	n/a
456	2024 Media Change	06/19/24	80,386.55	50.00	860.97	30.00	2,680	25 - 35	332
443	Meters RG3	06/30/24	13,638.89	50.00	137.88	37.50	364	35 - 40	346
444	Pump Station	07/02/24	75,617.62	50.00	756.18	37.50	2,016	35 - 40	321
454	2024 Fema Lines	07/03/24	192,640.00	50.00	1,915.87	62.50	3,082	50 - 75	343
447	Pump (Dyna Pump)	12/05/24	5,860.00	50.00	8.65	37.50	156	35 - 40	321
448	Fencing	12/12/24	3,250.00	10.00	17.76	37.50	87	35 - 40	390
Total			<u>\$ 1,891,701.55</u>		<u>\$ 1,891,701.55</u>		<u>\$ 38,934</u>		
(K1)									

⁸⁹ Remediated Application, ARF_Application_2023_Test_Year.pdf, Attachment 4, Schedule of Adjusted Operations, References, Adjustment C.

⁹⁰ Southern District's Response to Staff's Third Request, Item 8, 8_Depreciation_2024.pdf.

(L) Taxes other Than Income. Commission Staff calculated an \$11,978 increase in Taxes Other Than Income based on the increase in wages as shown in the table below.

Description	Amount
Wage Adjustments (Ref C1, C2)	\$ 156,581
Social Security Rate	0.0765
Total	<u>\$ 11,978</u>

Commission Staff recommends the Commission accept the proposed adjustment because the amount is known and measurable.

(M) Interest Income. Commission Staff made a \$6,540 adjustment to increase Interest Income in the Pro Forma SAO. Southern District did not report its interest income in the test year but properly reduced its calculated Total Revenue Requirement by \$6,540 when it calculated its Revenue Required from Water Sales. Therefore, there is no revenue impact from Commission Staff's adjustment, instead, the adjustment was made to include that amount in the Pro Forma SAO.

(N) Nonutility Income – Third Party Billings and Collections. Southern District provides monthly wastewater billing and collections to Prestonsburg City's Utilities Commission. It also provides monthly garbage fee billing and collections services to the Floyd County Fiscal Court. It retains three percent of collections for performing the services.⁹¹ Southern District did not report nonutility income in its test year in the SAO but it did reduce its calculated Total Revenue Requirement by \$14,373 (N1) for the income. Commission Staff reviewed Southern District's 2023 general ledger⁹² and determined that

⁹¹ Southern District's Response to Staff's Third Request, Item 22a

⁹² Southern District's Response to Staff's First Request, Item 1a, 1a_General_Ledger_2023.xlsx.

Southern District had not adjusted its income to reflect three percent of billings. Commission Staff increased nonutility income by \$14,162 (N2) to reflect the proper amount of income as shown in the table below. Commission Staff recommends the Commission accept the proposed adjustment because the amount is known and measurable.

Description	General Ledger Account No.	Test Year	Commission Staff Calculation	Adjustment
<i>Sewer Billings fbo Prestonsburg</i>				
Metered Sales - Residential Sewer	46150	\$ 67,487	\$ 67,487	\$ -
Metered Sales - Business Sewer	46151	32,434	32,434	0
PCUC Sewer Payments (3% of collections)	60003	(111,085)	(96,923)	14,162
sub-total		(11,164)	2,998	14,162
<i>Trash Collection Fees fbo Floyd Fiscal Court</i>				
Garbage Sales Revenue	47402	851,249	851,249	0
Solid Waste Payments (3% of collections)	60001	(825,712)	(825,712)	0
sub-total		25,537	25,537	0
Net Income		\$ 14,373	\$ 28,535	\$ 14,162
<i>Combined Billings and Collections</i>				
Collections		\$ 951,170	\$ 951,170	\$ -
Payments		(936,797)	(922,635)	14,162
Net (Income)		\$ 14,373	\$ 28,535	\$ 14,162
Income As Percent of Collections		1.5%	3.0%	
		(N1)		(N2)

OVERALL REVENUE REQUIREMENT

Southern District calculated its proposed revenue requirement based on the Debt Service Coverage (DSC) method. Commission Staff recommends using the Operating Ratio (OR) method to determine Southern District's revenue requirement as described below. This method will provide \$181,116 more cash flow annually to Southern District, which Commission Staff views as critical given Southern District's high water loss.

The Commission utilizes the Debt Service Coverage (DSC) and OR methods when evaluating a utility's revenue requirement. The Commission has historically applied the DSC method to calculate the Overall Revenue Requirement of water districts and water

associations.⁹³ 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;⁹⁴ (3) the average annual principal and interest payments on all long-term debts; and (4) working capital that is in addition to depreciation expense. The Commission applies the OR method⁹⁵ when there is no basis for a rate of return determination, the cost of the utility has largely been funded through contributions, or there is little or no outstanding long-term debt. Commission Staff recommends utilizing the OR as described below.

Debt Service Coverage

Southern District proposed the DSC method, utilizing average five-year debt service for 2025 through 2029 to calculate its revenue required from rates. Commission Staff's calculated increase using the DSC method compared to Southern District's application is shown in the Debt Service Coverage Method table below. Southern District

⁹³ Case No. 2022-00124, *Electronic Application of Elkhorn Water District for a Rate Adjustment Pursuant to 807 KAR 5:076* (Ky. PSC Oct. 24, 2022). 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 June 28, 2022).

⁹⁴ 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).

⁹⁵ Operating Ratio is defined as the ratio of expenses, including depreciation and taxes, to gross revenues. It is illustrated by the following equation:

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

submitted a modified rate study, as noted previously. The study included a corrected billing analysis which reflected a revised proposed revenue increase to \$185,529, or 5.28 percent. Since Southern District did not modify its application, the effect of the adjustment is reflected in Commission Staff's calculated increase in the table.

Description	Southern Water District Application	Commission Staff	
Pro Forma Operating Expenses	\$ 3,532,554	\$ 3,638,016	
Average Annual Principal and Interest Payments	261,384	322,503	(1)
Additional Working Capital at 20%	52,277	64,501	(2)
Total Revenue Requirement	3,846,215	4,025,020	
Other Revenue and Non Utility Income ()	(137,423)	(136,527)	
Interest Income ()	(6,540)	(6,540)	
Revenue Required From Water Sales	3,702,252	3,881,953	
Revenue from Sales at Present Rates ()	(3,212,927)	(3,297,287)	
Required Revenue Increase / (Decrease)	<u>\$ 489,325</u>	<u>\$ 584,666</u>	
Percentage Increase / (Decrease)	<u>15.23%</u>	<u>17.73%</u>	

1. Average Annual Principal and Interest Payments. Commission Staff reviewed the amortization schedules provided with the application as well as Southern District's 2023 Audited Financial Statements. Based on its review of the amortization schedules and the pending maturing of a loan at the end of 2027, it concluded that a three-year average debt service calculation is more appropriate because it better matches Southern District's cash flow requirements. Commission Staff's debt service calculations are shown in the table below.

Description	2025		2026		2027		2028		2029		Totals
	Principal	Interest & Fees	Principal	Interest & Fees	Principal	Interest & Fees	Principal	Interest & Fees	Principal	Interest & Fees	
Cobank Loan 2041	\$ 83,979	\$ 58,125	\$ 86,788	\$ 55,321	\$ 89,692	\$ 52,425	\$ 92,551	\$ 49,567	\$ 95,788	\$ 46,337	\$ 710,574
KIA B295-01	132,493	12,056	136,498	7,784	140,624	3,383	0	0	0	0	432,838
People's Bank	7,222	420	4,336	73	0	0	0	0	0	0	12,051
Cobank Loan	19,888	122	0	0	0	0	0	0	0	0	20,010
Community Trust Bank	14,409	221	0	0	0	0	0	0	0	0	14,630
Build America Bond	11,500	8,983	12,000	8,719	12,000	8,449	12,500	8,173	13,000	7,886	103,210
Totals	\$ 269,491	\$ 79,926	\$ 239,622	\$ 71,897	\$ 242,315	\$ 64,257	\$ 105,051	\$ 57,741	\$ 108,788	\$ 54,223	\$ 1,293,313
3-Year Average Debt Service					(1)	\$ 322,503					\$ 258,663
Additional Working Capital at 20%					(2)	\$ 64,501					\$ 51,733
3-Year Average Interest and Fees						\$ 72,027					

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. Commission Staff included \$64,501 in additional working capital.

Operating Ratio

A comparison of the revenue requirement utilizing Southern District's application and Commission Staff's calculations applied to the OR method is shown in the table below.

Operating Ratio Method

Description	Southern Water District	Commission Staff
Pro Forma Operating Expenses	\$ 3,532,554	\$ 3,638,016
Divided by: Operating Ratio	88%	88%
Subtotal	4,014,266	4,134,109
Plus: Interest Expense	65,215	72,027
Total Revenue Requirement	4,079,481	4,206,136
Other Revenue ()	(137,423)	(136,527)
Interest Income ()	(6,540)	(6,540)
Revenue Required From Rates	3,935,518	4,063,069
Revenue from Sales at Present Rates ()	(3,212,927)	(3,297,287)
Required Revenue Increase / (Decrease)	\$ 722,591	\$ 765,782
Percentage Increase / (Decrease)	22.49%	23.22%
Operating Ratio More / (Less) Than Debt Service Coverage	\$ 233,266	\$ 181,116
Percentage Increase from DSC Method	7.26%	5.49%

ADDITIONAL STAFF COMMENTS

Commission Staff recommends Southern District be required to file an Alternative Rate Filing no later than September 30, 2027, using 2026 as the test year. This will provide the Commission with a more in-depth oversight of Southern District's financial performance, liquidity, management and governance practices than can be achieved by just reviewing annual reports.

Signatures

/s/ Jeff Abshire

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

/s/ Jason Green

Prepared by: Jason Green
Rate Design Branch
Division of Financial Analysis

APPENDIX A

APPENDIX TO COMMISSION STAFF'S REPORT OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2024-00251 DATED JUN 16 2025

* Denotes Rounding

Nonrecurring Charges Adjustments

Connection/Turn-On Charge			
	Utility Revised Charge	Staff Revised Charge	
Field Materials	\$ -	\$ -	
Field Labor	\$ -	\$ -	
Office Supplies	\$ -	\$ -	
Office Labor	\$ 12.16	\$ -	
Transportation	\$ 11.00	\$ 11.00	
Misc.	\$ -	\$ -	
Total Revised Charge*	\$ 23.16	\$ 11.00	

Current Rate \$20.00

Connection/Turn-On Charge (After Hours)

	Utility Revised Charge	Staff Revised Charge	
Field Materials	\$ -	\$ -	
Field Labor	\$ 72.99	\$ 72.99	
Office Supplies	\$ -	\$ -	
Office Labor	\$ 6.08	\$ -	
Transportation	\$ 11.00	\$ 11.00	
Misc.	\$ -	\$ -	
Total Revised Charge*	\$ 90.07	\$ 84.00	

Current Rate \$88.00

Meter Relocation Charge

	Utility Revised Charge	Staff Revised Charge	
Field Materials	\$ -	\$ -	
Field Labor	\$ -	\$ -	
Office Supplies	\$ -	\$ -	
Office Labor	\$ -	\$ -	
Transportation	\$ -	\$ -	
Misc.	\$ -	\$ -	
Total Revised Charge*	Actual Cost	Actual Cost	

Current Rate Actual Cost

Meter Re-read Charge			
	Utility Revised Charge		Staff Revised Charge
Field Materials	\$	-	\$ -
Field Labor	\$	-	\$ -
Office Supplies	\$	-	\$ -
Office Labor	\$	12.16	\$ -
Transportation	\$	11.00	\$ 11.00
Misc.	\$	-	\$ -
Total Revised Charge	\$	23.16	\$ 11.00
Current Rate		\$20.00	

Meter Test Charge			
	Utility Revised Charge		Staff Revised Charge
Field Materials	\$	50.00	\$ 50.00
Field Labor	\$	72.99	\$ -
Office Supplies	\$	5.00	\$ 5.00
Office Labor	\$	-	\$ -
Transportation	\$	11.00	\$ 11.00
Misc.	\$	15.00	\$ 15.00
Total Revised Charge	\$	153.99	\$ 81.00
Current Rate	\$	50.00	

Reconnection Charge			
	Utility Revised Charge		Staff Revised Charge
Field Materials	\$	-	\$ -
Field Labor	\$	-	\$ -
Office Supplies	\$	-	\$ -
Office Labor	\$	12.16	\$ -
Transportation	\$	11.00	\$ 11.00
Misc. (Bank Charge)	\$	-	\$ -
Total Revised Charge	\$	23.16	\$ 11.00
Current Rate	\$	20.00	

Reconnection Charge (After Hours)			
	Utility Revised Charge		Staff Revised Charge
Field Materials	\$	-	\$ -
Field Labor	\$	72.99	\$ 72.99
Office Supplies	\$	15.00	\$ 15.00
Office Labor	\$	6.08	\$ -
Transportation	\$	11.00	\$ 11.00
Misc.	\$	-	\$ -
Total Revised Charge*	\$	105.07	\$ 99.00
Current Rate	\$	88.00	

Returned Check Charge			
	Utility Revised Charge		Staff Revised Charge
Field Materials	\$	-	\$ -
Field Labor	\$	-	\$ -
Office Supplies	\$	15.00	\$ 15.00
Office Labor	\$	12.16	\$ -
Transportation	\$	-	\$ -
Misc.	\$	-	\$ -
Total Revised Charge*	\$	27.16	\$ 15.00
Current Rate	\$	10.00	

Service Call/Investigation Charge			
	Utility Revised Charge		Staff Revised Charge
Field Materials	\$	-	\$ -
Field Labor	\$	-	\$ -
Office Supplies	\$	-	\$ -
Office Labor	\$	12.16	\$ -
Transportation	\$	11.00	\$ 11.00
Misc.	\$	-	\$ -
Total Revised Charge*	\$	23.16	\$ 11.00
Current Rate	\$	20.00	

Service Call/Investigation Charge (After Hours)			
	Utility Revised Charge		Staff Revised Charge
Field Materials	\$	-	\$ -
Field Labor	\$	72.99	\$ 72.99
Office Supplies	\$	-	\$ -
Office Labor	\$	6.08	\$ -
Transportation	\$	11.00	\$ 11.00
Misc.	\$	-	
Total Revised Charge	\$	90.07	\$ 84.00

Current Rate \$ 88.00

Disconnection Charge (New Charge)			
	Utility Revised Charge		Staff Revised Charge
Field Materials	\$	-	\$ -
Field Labor	\$	24.33	\$ -
Office Supplies	\$	-	\$ -
Office Labor	\$	12.16	\$ -
Transportation	\$	11.00	\$ 11.00
Misc.	\$	-	\$ -
Total Revised Charge	\$	47.49	\$ 11.00

Current Rate N/A

APPENDIX B

APPENDIX TO COMMISSION STAFF'S REPORT OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2024-00251 DATED JUN 16 2025

The following rates and charges are recommended by Commission Staff based on the adjustments in Commission Staff's Report for the customers in the area served by Southern Water and Sewer District. All other rates and charges not specifically mentioned herein shall remain the same.

Monthly Water Rates

Customer Charge	\$ 14.04	Minimum bill
First 2,000 gallons	0.01503	per gallon
All Over 2,000 gallons	0.01156	per gallon
Wholesale Rate	0.00595	per gallon

Nonrecurring Charges

Connection/Turn-on Charge	\$11.00
Connection/Turn-on Charge (After Hours)	\$84.00
Meter Re-read Charge	\$11.00
Meter Test Charge	\$81.00
Reconnection Charge	\$61.00
Reconnection Charge (After Hours)	\$99.00
Returned Check Charge	\$15.00
Service Call/Investigation	\$11.00
Service Call/Investigation (After Hours)	\$84.00
Disconnection Charge	\$11.00
Tap On Fee – 3/4-Inch Meter	\$1,548.00
Tap On Fee – 3/4 x 5/8-Inch Meter	\$1,885.00
Tap On Fee – 2-Inch Meter	\$5,500.00

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