

COMMONWEALTH OF KENTUCKY
BEFORE THE UTILITY REGULATORY COMMISSION

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In the Matter of:

NOTICE OF ADJUSTMENT OF THE RATES)	
OF KENTUCKY-AMERICAN WATER COMPANY)	CASE NO.
EFFECTIVE ON AND AFTER APRIL 18,)	7783
1980)	

O R D E R

On March 26, 1980, Kentucky-American Water Company, the Applicant, filed a Notice of an adjustment of water service rates to become effective on April 18, 1980. The proposed rates would increase annual operating revenues to the Company by \$1,201,666, or approximately 12.85%.

To determine the reasonableness of the requested rates, the Commission in an Order dated March 26, 1980, set a public hearing to be held May 6, 1980, and suspended the proposed rates for a period of five (5) months on and after the effective date. Further hearings were held July 1, 1980, and July 31, 1980. Notice of such hearings were made by the Applicant in manners prescribed by Kentucky Revised Statutes and the Commission's rules and regulations. The only party intervening in this matter was the Attorney General's Division of Consumer Intervention.

Briefs from the parties of interest were filed by August 25, 1980, and the entire record was then submitted to the Commission for final determination.

The Kentucky-American Water Company operates as a public utility providing water service to approximately 61,000 customers in five counties of Central Kentucky. The Company is a wholly-owned subsidiary of the American Water Works Company, Inc., and as such benefits from various parent subsidiary relationships.

TEST YEAR

The Commission accepts the Applicant's proposed test period, the calendar year ending December 31, 1979, for the purpose of determining the reasonableness of the proposed rates and charges. In accordance with Commission policy, pro-forma adjustments have been included when known, just and measurable.

VALUATION METHODS

Net Investment

The Commission has determined that at the end of the test period the Applicant's Net Investment in its utility operations is as follows:

Utility Plant in Service	\$50,912,658
Construction Work in Progress	440,060
Prepayments	17,792
Materials and Supplies	198,200
Cash Working Capital	<u>591,455</u>
Sub-total	\$52,160,165
Less:	
Reserve for Depreciation and Amortization	\$ 6,889,034
Customer Advances for Construction	2,446,240
Contributions	3,040,920
Deferred Federal and State Taxes	2,898,123
3% Investment Tax Credit	<u>284,813</u>
Sub-total	\$15,559,130
Net Original Cost Rate Base	\$36,601,035
Less:	
Plant Acquisition Adjustment	<u>\$ 1,511,937</u>
Net Investment	<u><u>\$35,089,098</u></u>

The Applicant's proposed Net Original Cost Rate Base of \$35,371,000¹ has been accepted with four exceptions. The proposal to include the non-revenue producing committed construction program of \$446,754² with related additional depreciation and deferred income taxes of \$4,548 and \$33,789, respectively, are in the Commission's opinion not proper items for rate-making purposes

¹Applicant's Notice, Exhibit 6, Schedule 1, page 1.

²Applicant's Notice, Exhibit 6, Schedule 2.

and have not been included in the Net Original Cost Rate Base calculation. However, some portions of such program are included in Construction Work in Progress of \$440,060 which has been included in the Commission's above-determined calculation. In conformity with Commission policy, cash working capital is computed as one-eighth of adjusted operation and maintenance expense and the Reserve For Depreciation and Amortization increased by \$25,850 to include an end-of-period depreciation expense adjustment.

Capital Structure

Applicant proposed a capital structure of \$34,638,582. The Commission has accepted this capital structure and has allocated the Job Development Credit (JDIC) to the other capital components based on their relative weights to total capital excluding JDIC in compliance with Internal Revenue Service regulations. This method, in further calculation, assigns the overall cost of capital to JDIC.

Therefore, the Commission finds Applicant's capital structure as of December 31, 1979 to be as follows:

	<u>\$</u>	<u>%</u>
Long-Term Debt	\$20,438,215	57.39%
Short-Term Debt	1,980,074	5.56
Preferred Stock	4,109,723	11.54
Common Equity	9,084,838	25.51
	<u>\$35,612,850</u>	<u>100.00%</u>

The Commission is aware of other valuation methods not included in the evidence of record. The Commission has given due consideration to all elements of value in determining the reasonableness of the matter herein.

REVENUES AND EXPENSES

The Applicant proposed several pro forma adjustments to reflect more current operating conditions. The Commission is of the opinion that the adjustments generally are proper and have been accepted with the following exceptions.

The Commission has deleted all adjustments related to the non-revenue producing committed construction program. The Utility Regulatory Commission assessment included herein is calculated

using the actual Fiscal Year 1980-1981 assessment rate. This reduces Applicant's proposed adjustment by \$3,569. Applicant further proposed to increase interest expenses on short-term debt by \$216,519 based on test-year end interest rates. The Commission has reduced this proposed adjustment by \$81,813 to \$134,706 in order to more accurately reflect current interest rates and current market conditions. Federal and State Income Taxes have been computed on the adjusted corporate income level and Applicant's proposed reduction decreased by \$108,090. Finally, the Commission rejects the Applicant's proposed adjustments to other income and miscellaneous deductions.

The Commission has made two further adjustments to the Applicant's Income Statement. First, the Commission has included an Allowance For Funds Used During Construction of \$9,232 in operating revenues. Second, the Commission has deducted \$3,500 of institutional advertising from operating expenses.

Therefore, Applicant's test period operations are adjusted as follows:

	<u>Actual</u>	<u>Adjustments</u>	<u>Adjusted</u>
Operating Revenues	\$9,218,495	\$138,819	\$9,357,314
Operating Expenses	<u>6,467,683</u>	<u>127,160</u>	<u>6,594,843</u>
Net Operating Income	<u>\$2,750,812</u>	<u>\$ 11,659</u>	<u>\$2,762,471</u>

RATES OF RETURN

The Commission is of the opinion that an 8.5% return on Net Investment is proper in this case and that such a return will permit Kentucky-American to provide for its necessary operating expenses, pay its interest, pay its dividend on preferred stock, provide for a reasonable dividend on its common stock plus a reasonable amount of surplus for equity growth.

The rates prescribed in Appendix "A" will produce annual operating revenues of approximately \$9,823,200. These rates will further provide net operating income levels of \$2,998,600 on a test period basis, and are the levels of net operating income found

reasonable in this matter. As a result, test period operations result in a net operating income deficiency of \$236,100. This deficiency adjusted for income taxes results in additional revenue requirements of \$465,900, and is the amount of additional revenue granted herein.

These additional revenues should provide the following approximate rates of return on the various valuation methods and, in our opinion, are the reasonable levels of return for the Kentucky-American Water Company.

<u>Valuation Base</u>	<u>Amount</u>	<u>Rate of Return</u>
Net Original Cost Rate Base	\$36,601,035	8.19%
Net Investment	35,089,098	8.54%
Capital Structure	35,612,850	8.42%
Common Equity	9,084,838	12.00%

SUMMARY

The Commission, after consideration of all the evidence of record and being advised, is of the opinion and so FINDS that the rates prescribed in Appendix "A" producing gross operating revenues of \$9,823,200 for the adjusted test year ending December 31, 1979, are the fair, just and reasonable rates to be charged for water service by Kentucky-American Water Company.

The Commission further FINDS, that the returns allowed in this matter on a test period basis will permit the Applicant to provide for its operating expenses, pay its interest, provide for a reasonable dividend and a reasonable amount of surplus for equity growth.

The Commission further FINDS, that the rates proposed by the Applicant are unfair, unjust, and unreasonable in that they produce annual revenues in excess of those found reasonable herein and should be denied.

IT IS THEREFORE ORDERED, that the proposed rates sought by the Applicant as set out in the Application be and the same are hereby denied.

IT IS FURTHER ORDERED, that the rates set forth in Appendix "A" be and are hereby approved as the fair, just and reasonable rates for water service provided by Kentucky-American Water Company effective the date of this Order.

IT IS FURTHER ORDERED, that the Kentucky-American Water Company file with this Commission within thirty (30) days from the date of this Order its revised tariff sheets setting out the rates for water service approved herein.

Done at Frankfort, Kentucky, this 18th day of September, 1980.

UTILITY REGULATORY COMMISSION

Chairman

Vice Chairman

Commissioner

ATTEST:

Secretary

APPENDIX "A"

APPENDIX TO AN ORDER OF THE UTILITY REGULATORY
COMMISSION IN CASE NO. 7783 DATED SEPTEMBER 18, 1980.

The following rates and charges are prescribed for the customers in the area served by the Kentucky-American Water Company. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of the Commission prior to the date of this Order.

Service Classification No. 1

<u>Rates</u>	<u>Cubic Feet Per Month</u>	<u>Quarter</u>	<u>Rate Per 100 Cubic Feet</u>
For the First	5,000	15,000	\$0.96973
For the Next	30,000	90,000	0.70231
For the Next	300,000	900,000	0.40813
For All Over	335,000	1,005,000	0.26976

Minimum Charges

<u>Size of Meter</u>	<u>Minimum Month</u>	<u>Charge Per Quarter</u>
5/8"	\$ 2.88	\$ 8.64
3/4"	4.33	12.99
1"	7.18	21.54
1½"	14.43	43.29
2"	23.08	69.24
3"	49.90	149.70
4"	76.16	228.48
6"	160.25	480.75

Service Classification No. 2

<u>Meter Rates</u>	<u>Rate Per 100 Cubic Feet</u>
For all water used	\$0.49068

Service Classification No. 3

<u>Rates</u>	<u>Rate Per Annum</u>
<u>Size of Service</u>	
4" Diameter	\$114.00
6" Diameter	226.80
8" Diameter	454.68
12" Diameter	909.48

Service Classification No. 4

Rates

Rate
Per Annum

For each public fire hydrant, contracted for or ordered by City, County, State or Federal Governmental Agencies or Institutions	\$112.80
For each private fire hydrant contracted for by industries or private institutions	112.80
For each water customer whose premises is located within 1,000 feet of a private hydrant not contracted for by industries or private institutions, as measured along public streets or roads, in advance	4.92

Service Classification -
Public, Private, Fire Protection
(West Scott County Division)

Rates

Rate
Per Annum

For each public fire hydrant, contracted for by City, County, State or Federal Governmental Agencies or Institutions	\$25.00
For private fire connections used exclusively for fire protection purposes.	

<u>Size of Service</u>	<u>Rate</u> <u>Per Annum</u>
4" Diameter	\$108.72
6" Diameter	216.36
8" Diameter	433.80
12" Diameter	867.63

Reconnection Charge

When it has been necessary to discontinue water service to any premises because of a violation of the Company's Rules and Regulations on account of non-payments of any bill for water service, a charge of Ten Dollars (\$10.00) will be made to cover the expense of turning on the water service.