

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

PURCHASED WATER ADJUSTMENT OF)
PEAKS MILL WATER DISTRICT) CASE NO. 6060-1

O R D E R

On July 18, 1984, the Peaks Mill Water District ("Peaks Mill") filed an application with the Commission for approval to increase the rates charged to its customers in accordance with the provisions of its purchased water adjustment clause on file with the Commission. Effective August 1, 1984, Peaks Mill's supplier, the City of Frankfort, Franklin County, Kentucky, ("City") increased its wholesale price of water by \$.39 per thousand gallons. The increase in water cost for water purchased by Peaks Mill directly from the City is \$19,417 on an annual basis.

COMMENTARY

Prior to approving increased rates resulting from purchased water cost increases pursuant to 807 KAR 5:067, the Commission must examine an applicant's financial condition to determine whether it can absorb any of the increased cost. If there is potential for absorption, the Commission may adjust rates to offset only that portion of the increased water cost which cannot be absorbed.

TEST PERIOD

In order to determine the reasonableness of the proposed purchased water adjustment and the increase in rates, the Commission has adopted the 12-month period ended December 31, 1983, as the test period in this matter. Adjustments deemed proper and reasonable have been included to more accurately reflect current operating conditions.

REVENUES AND EXPENSES

The rates proposed by Peaks Mill will increase revenues by \$19,317¹ to offset the increased cost of purchased water. No other adjustments were proposed. The Commission has made the following adjustments to expenses, in conformance with its rate-making policy, to more fairly represent the actual operating expenses of Peaks Mill:

Depreciation Expense

Peaks Mill's test period depreciation expense was \$16,997. This reflects depreciation on total plant using a composite rate of approximately 2.6 percent.² The Commission's policy is to compute depreciation expense for rate-making purposes on the basis of original cost of the plant in service less contributions in aid of construction. The balance sheet filed by Peaks Mill shows contributions in aid of construction at the end of the test period

¹ 1983 gallons (41,100,000) X PWA application rate (\$.47/1000 gallons) = \$19,317.

² \$16,997 ÷ \$657,731 = 2.58 percent.

to be \$381,529. This amount is approximately 58 percent of the total cost of the utility plant in service. In determining the pro forma depreciation expense, the Commission has utilized the depreciation rate applied by Peaks Mill and has excluded depreciation associated with contributed property. The adjusted depreciation expense for rate-making purposes is \$7,210.³

The Commission has further adjusted operating expenses to reflect the increase in purchased water cost of \$19,417 from Peaks Mill's supplier. Therefore, the Commission finds that Peaks Mill's adjusted test period operations are as follows:

	<u>Actual</u>	<u>Adjustments</u>	<u>Adjusted</u>
Operating Revenues	\$115,899		\$115,899
Operating Expenses	<u>86,820</u>	<u>\$ 9,630 4</u>	<u>96,450</u>
Operating Income	<u>\$ 29,079</u>	<u>\$ <9,630></u>	<u>\$ 19,449</u>

Line Loss

In testing the absorption potential for Peaks Mill it has come to the Commission's attention that a substantial portion, 20

3	Total Plant	\$658,831
	Less Contributions in Aid of Construction	<u>381,529</u>
	Non-contributed Plant	\$277,302
	Composite Rate	<u>X 2.6%</u>
	Depreciation allowed for rate-making purpose	\$ 7,210
4	Depreciation adjustment	\$ <9,787>
	Purchased Water Adjustment	<u>19,417</u>
	Net Adjustment	\$ 9,630

percent,⁵ of Peaks Mill's purchased water was not actually sold to customers. Commission policy in the past has been to allow a 15 percent water loss for rate-making purposes. Although the Commission realizes that 7 percent of the purchased gallons was used for fire protection and, accordingly, made no adjustment for water loss in this proceeding, the Commission is of the opinion that this amount of unbilled water for fire protection is abnormal. In order for Peaks Mill's purchased water expenses to qualify for rate-making purposes in future cases, adequate records detailing all water usage should be maintained.

REVENUE REQUIREMENTS

Peaks Mill's annual debt service based on outstanding debt at the end of the test period is \$11,000.⁶ Peaks Mill's adjusted net operating income of \$19,449 plus interest income from water operations of \$15,634 provides a debt service coverage of approximately 3.19X. The Commission is of the opinion that a debt service coverage of 1.2X is fair, just and reasonable, and further that a debt service coverage of 3.19X is more than adequate to enable Peaks Mill to pay its operating expenses and to meet the

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	<u>Gallons</u>
1983 Water Sales	41,099,900
Free Customers (Fire Departments)	3,500,000
Unaccounted for Water	6,895,700
Total Gallons Purchased	51,495,600

$$(3,500,000 + 6,895,700) \div 51,495,600 = 20 \%$$

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Bonds (5-year average principal 1984 - 1988)	\$ 4,000
Interest (5-year average interest 1984 - 1988)	7,000
Debt Service	\$11,000

requirements of its lenders. Therefore, the Commission is of the opinion that Peaks Mill has the potential to fully absorb its increased cost of water.

SUMMARY

The Commission, after consideration of the evidence of record and being advised, is of the opinion and finds that:


1. Peaks Mill has the potential to fully absorb the increase in purchased water cost.


2. The rates of Peaks Mill in effect under authority of the Commission prior to this date should continue in effect.

IT IS THEREFORE ORDERED that the rates requested by Peaks Mill be and they hereby are denied.

Done at Frankfort, Kentucky, this 4th day of October, 1984.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Secretary