

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

\* \* \* \* \*

In the Matter of

THE ADJUSTMENT OF RATES OF )  
THE OKOLONA SEWER CONSTRUCTION )  
DISTRICT OF JEFFERSON COUNTY, )  
KENTUCKY )

CASE NO.  
8751

ORDER

IT IS ORDERED That the Staff Report dated March 15, 1984, attached hereto and made a part hereof (Appendix A) be, and it hereby is, made a part of the record in this case.

IT IS FURTHER ORDERED That the parties herein shall have until the close of business April 6, 1984, to submit written comments or to request a hearing with respect to the matters in the Report.

Done at Frankfort, Kentucky, this 26th day of March, 1984.

PUBLIC SERVICE COMMISSION

  
For the Commission

ATTEST:

\_\_\_\_\_  
Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 8751 DATED 3/26/84

MEMORANDUM

TO: The Commission  
FROM: Gary L. Forman  
DATE: March 15, 1984  
RE: Case No. 8751 - Okolona Sewer Construction District  
Adjustment to Depreciation Expense

In the final Order in the above case, issued on October 27, 1983, the Commission adjusted the annual depreciation expense of Okolona Sewer Construction District ("Okolona") to exclude depreciation on property constructed with the proceeds of water revenue assessment bonds. The Commission further adjusted depreciation to exclude the amount of depreciation associated with the reported level of contributions in aid of construction. In the determination of the allowable depreciation expense for rate-making purposes the actual test-period depreciation expense was increased by \$1,086 to include depreciation on the cost of utility plant additions erroneously reported in operation and maintenance expenses during the test period. Depreciation of \$58,393 on plant constructed with the proceeds of "assessment issues" was also excluded. The resulting depreciation expense of \$160,979 was then reduced by \$41,855 or 26 percent based on the ratio of reported contributions in aid of construction of \$1,420,986 to adjusted plant purchased with revenue fund issues of \$5,401,835. The calculations supporting the depreciation adjustment are shown in GLF - EXHIBIT I, hereto.

In its petition for rehearing, Okolona contended that the Commission should not have disallowed \$40,686 of depreciation associated with the test year-end level of contributions in aid of construction because \$1,362,524 of the year-end contributions in aid of construction was representative of retired assessment bonds, which resulted in a double reduction of depreciation expense.

On December 5, 1983, the Commission granted a rehearing in this matter to further investigate the level of depreciation allowed in the October 27, 1983 Order. I have reviewed the record in this matter, including the information submitted in response to the request for additional information dated January 10, 1984. In my opinion the determination of depreciation expense for rate-making purposes included in the Order of October 27, 1983, was appropriate, based on the evidence contained in the record at that time, and consistent with the Commission's policy on allowable depreciation for rate-making purposes. The sources of the \$1,420,986 of test year-end contributions in aid of construction were not identified by Okolona until the petition for rehearing was filed. Theoretically, Okolona is correct in that depreciation associated with plant constructed with proceeds of assessment issues was taken out twice. However, the additional information contained in the petition for rehearing and the response to the information request of January 10, 1984 reveals that the allowed depreciation of \$119,124 is actually overstated due to the fact that contributions in aid of construction at the end of the test

period does not include all funds provided at no cost to Okolona.

Based on information contained in the record in this case, Okolona's primary sources of funds for capital construction are: Proceeds from Assessment Bond Issues, Proceeds from Sewer Revenue Bond Issues, Federal Grants, and General Revenue Funds. Other plant was provided at no cost to Okolona through Lien and Refunding Agreements, and Direct Contributions or "Donated Lines". Although it is difficult at best to trace total utility plant back to the exact sources of funds used for construction purposes, in this proceeding Okolona provided a breakdown of its total plant in service of \$8,587,556 into plant funded with Assessment Issues of \$2,966,842 and plant funded with Revenue Issues of \$5,620,714. Likewise, based on the depreciation schedule contained in Application Exhibit 8, Okolona identifies depreciation expense with these two categories of plant. In the original Order in this matter the Commission disallowed \$58,393 of actual test-period depreciation on plant funded with Assessment Issues. (This reduction was not contested by Okolona in its petition for rehearing.) The plant funded by Revenue Issues, included one item of "Plant in Process of Reclassification" of \$224,309 on which no depreciation was accrued during the test period. Therefore, the actual test-period depreciation on Revenue Issues was based on Plant in Service of \$5,396,405. Okolona's actual test-period depreciation expense was \$159,893, exclusive of depreciation on plant funded with assessment issues.

In determining the amount of depreciation on contributed property, the Commission would generally use the reported level of contributions in aid of construction from the utility's balance sheet. However, since the level of contributions reported by Okolona does not reflect all contributions, an analysis of the sources of funds for construction was required. In response to the Commission's request for information of January 10, 1984, Okolona provided a detailed breakdown in Item No. 1 of contributions in aid of construction, and, in Item No. 4, of Funding Sources for Revenue Bond Accounts of \$5,620,714.

From the analysis of the funding sources, I have attempted to determine the actual amount of contributed property as of September 30, 1982. Using the information contained in the record in this case, GLF - EXHIBIT II reflects my calculation of the appropriate level of contributions in aid of construction. First, I have taken the level of contributions in aid of construction as reported by Okolona of \$1,420,986. An analysis of this amount reflects that \$1,140,000 represents retired assessment bonds and \$264,122 represents repayments of lien and refunding agreements. Federal Grants of \$58,462 were also included in the September 30, 1982 contributions in aid of construction account. Based on the information contained in the response to Item No. 4 of the January 10, 1984 information request, \$1,863,669 of donated lines, and \$987,968 of federal assistance not previously included in contributions in aid of construction should be added to the September 30, 1982 balance. The items contained in response to

Item No. 3 to the Commission's January 10, 1984 information request totaling \$64,912 should also be included in contributions in aid of construction since these were direct contributions which were previously recorded as revenues and not credited to contributions in aid of construction. These three items total \$2,916,549, which is the amount by which contributions in aid of construction are understated at the end of the test period. This results in adjusted contributions in aid of construction of \$4,337,535.

If contributions in aid of construction are re-stated based on my analysis the resulting allowable depreciation expense would be \$74,050 as determined on GLF - EXHIBIT III, hereto. On Exhibit III the same methodology has been used to calculate the allowed depreciation as in the original order. Depreciation on assets purchased with Assessment Issues of \$58,393 has been excluded and the increase in plant and depreciation expense for the items erroneously expensed has been reflected. In determining the amount of contributions in aid of construction associated with plant funded with revenue issues, I have reduced the adjusted contributions in aid of construction for rate-making purposes by \$1,140,000 which is representative of the retired assessment bonds and by the amount of \$264,122 associated with the Lien and Refunding Agreements. The resulting ratio of contributed property to total plant in service for rate-making purposes is 54 percent. Therefore, 46 percent or \$74,050 of the \$160,979 of test-year depreciation should be allowed for rate-making purposes.

Memorandum to the Commission  
March 15, 1964  
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In my opinion the books of Okolona should be adjusted to properly state contributions in aid of construction in accordance with accounting requirements of the Uniform System of Accounts for Sewer Utilities prescribed by this Commission. Furthermore, the findings of the Commission in the Order on rehearing should be adjusted to decrease the revenue requirements of Okolona by \$74,050 and the final rates should be adjusted accordingly.

OKOLONA SEWER CONSTRUCTION DISTRICT  
CASE NO. 8751

## Adjustment to Depreciation

Test Year Depreciation Expense<sup>1/</sup>

Source of Funds	Cost	Depreciation Expense September 30, 1982
Assessment Issues	\$2,966,842	\$ 58,393
Revenue Issues	<u>5,620,714</u>	<u>159,893</u>
Total	<u>\$8,587,556</u>	<u>\$218,283</u>
		<u>Depreciation Expense</u>
Total - Revenue Issues	\$5,620,714	\$159,893
Less: Plant in Process of Reclassification	224,309 <sup>2/</sup>	-
Add: Capitalized Items Per Order	<u>5,430<sup>3/</sup></u>	<u>1,086</u>
Adjusted Plant (Revenue Issues)	<u>\$5,401,835</u>	<u>\$160,979</u>

Contributions in Aid of Construction ("CIAC")

$$\frac{\text{CIAC 9/30/82}}{\text{Adjusted Plant}} = \frac{1,420,986^{4/}}{5,401,835} = 26\%$$

Adjusted Depreciation (above)	\$ 160,979
CIAC as a Percent of Adjusted Plant	<u>X 26%</u>
Depreciation on Contributed Property	<u>\$ 41,855</u>
Adjusted Depreciation	\$ 160,979
Less: Depreciation on Contributed Property	<u>41,855</u>
Allowable Depreciation	<u>\$ 119,124</u>

<sup>1/</sup> Application, Exhibit 8.<sup>2/</sup> Ibid.<sup>3/</sup> October 27, 1983 Order, p. 13.<sup>4/</sup> Response to February 2, 1983 Information Request, Item No. 16.



OKOLONA SEWER CONSTRUCTION DISTRICT  
CASE NO. 8751

Adjustment to Depreciation

Sources of Funds for Utility Plant

"Assessment Issues"	\$2,966,842
Assessment Bonds, Lien and Refund Agreements	
"Revenue Issues" <sup>1/</sup>	
Donated Lines	\$1,863,669
Federal Assistance	1,046,430
District Revenues	835,615
Bond Proceeds	1,875,000
Total	<u>\$5,620,714</u>
Total Plant in Service 9/30/82	<u>\$8,587,556</u>

Adjusted Contributions in Aid of Construction ("CIAC")

CIAC Per Books 9/30/82:

Retired Bonds	\$1,140,000
Repayments L & R Agreements	264,122
Donated Lines	4,500
Excess Bond Transfers	<57,942>
Net Interest Earned	11,844
Federal Grants	58,462
	<u>\$1,420,986</u>

Additional CIAC Not Included  
in 9/30/82 Balance:

Donated Lines	\$1,863,669 <sup>2/</sup>	
Federal Assistance	987,968 <sup>3/</sup>	
Receipts from Others	<u>64,912<sup>3/</sup></u>	<u>\$2,916,549</u>

Adjusted CIAC 9/30/82	<u>\$4,337,535</u>
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<sup>1/</sup> Response to January 10, 1984 Information Request, Item No. 4.

<sup>2/</sup> Federal Assistance	\$1,046,430
Less: Federal Grants Credited to CIAC as of 9/30/82	58,462
Federal Assistance Not Included in CIAC	<u>\$ 987,968</u>

<sup>3/</sup> Response to January 10, 1984 Information Request, Item No. 3.

OKOLONA SEWER CONSTRUCTION DISTRICT  
CASE NO. 8751

## Adjustment to Depreciation

Test Year Depreciation Expense<sup>1/</sup>

Source of Funds	Cost	Depreciation Expense September 30, 1982
Assessment Issues	\$2,966,842	\$ 58,393
Revenue Issues	5,620,714	159,893
Total	<u>\$8,587,556</u>	<u>\$218,283</u>

		Depreciation Expense
Total - Revenue Issues	\$5,620,714	\$159,893
Less: Plant in Process of Reclassification	224,309	-
Add: Capitalized Items Per Order	5,430	1,086
Adjusted Plant (Revenue Issues)	<u>\$5,401,835</u>	<u>\$160,979</u>

Ratio of Contributions in Aid of Construction ("CIAC") to Total Plant

Adjusted CIAC		\$4,337,535
Less: Lien and Refunding Agreements	264,122	
Retired Bonds	<u>1,140,000</u>	<u>1,404,122</u>
CIAC for Rate-Making Purposes		<u>\$2,933,413</u>
	<u>Adjusted CIAC</u>	\$ 2,933,413
	Adjusted Plant (per above)	\$ 5,401,835 = 54%

Allowable Depreciation:

Depreciation Expense Exclusive of Assessment Issues	\$160,979
Less: Portion Associated With Contributed Property (54%)	86,929
Allowable Depreciation Expense	<u>\$ 74,050</u>

Adjustment to October 27, 1983 Order:

Allowed Depreciation	\$119,124 <sup>2/</sup>
Allowable Depreciation (per above)	74,050
Required Adjustment to Depreciation Expense	<u>\$ 45,074</u>

<sup>1/</sup> Application, Exhibit 8.<sup>2/</sup> October 27, 1983 Order, p. 20.