COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

AN ADJUSTMENT OF RATES OF PARKSVILLE WATER DISTRICT	))	CASE NO. 8907

O R D E R

On September 19, 1983, Parksville Water District ("Parksville") filed an application with this Commission requesting authority to adjust its rates pursuant to 807 KAR 5:076, Alternative Rate Adjustment Procedure for Small Utilities ("ARF"). The rates proposed by Parksville would produce additional annual revenues in the amount of $46,616, reflecting an increase of 38.9 percent above the level of actual test-period revenues.

An examination of the comparative income and expense statement which Parksville submitted with its application revealed that the format of the statement, as well as the account classifications contained therein, did not comply with the Uniform System of Accounts for Class C and D Water Utilities. Therefore, by its Order dated November 2, 1983, the Commission required Parksville to submit a revised comparative income and expense statement in accordance with the Commission's prescribed reporting requirements. This information was filed on November 18, 1983.

Also submitted in Parksville's application were a billing analysis based upon the number of gallons sold during an average month and a schedule reflecting actual monthly water purchases and sales. An examination of the water purchases and sales schedule revealed substantial monthly fluctuations in the number of gallons of water sold; hence, the Commission determined that Parksville's billing analysis did not accurately reflect test-period water sales or the revenues to be produced from those sales. Therefore, the Commission, in its Order dated January 10, 1984, required Parksville to submit a revised billing analysis which would reflect the application of its current and proposed rates to the actual number of gallons of water sold. Parksville filed this information with the Commission on February 13, 1984. As a result of these revisions to its application, the revenue increase requested by Parksville was amended to an amount of $38,617 which reflected an increase of 35.8 percent above actual test-period revenues.

According to the revised income and expense statement, Parksville realized total test-period revenues in the amount of $101,541 from the metered sales of water to its general customers. However, the revised billing analysis revealed the total amount of Parksville's test-period water sales to be $107,353, based upon the actual number of gallons of water sold. Therefore, to reflect the total amount of revenue calculated per the billing analysis, the Commission has adjusted Parksville's test-period revenues in the amount of $5,812. Parksville's revenues have also been increased by $1,750 to reflect the amount of additional annual revenue that will be generated from bulk sales of water. In addition, Parksville's test-period revenues have been reduced by

$3,725 to reflect the amount of connection charges erroneously reported as revenue. These adjustments, combined with Parksville's other revenue of $2,605, resulted in normalized test-period revenues in the total amount of $111,708.[1] Based upon the determination herein, Parksville will be allowed to increase its rates to produce additional annual revenues of $9,289, thereby reflecting an increase of 8.3 percent above adjusted test-period revenue.

On January 20, 1984, an informal conference was held at the Commission's offices in Frankfort, Kentucky, between members of the Commission staff and representatives of Parksville and the Bluegrass Area Development District ("BADD"), the preparers of the rate adjustment application. This meeting, held at the request of Parksville, was for the purpose of the clarification of various items contained in the rate application. There were no intervenors in this matter.

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	Test-Period Actual	Normalization Adjustments	Adjusted Test-Period
Operating Revenues:			
Metered Sales to General Customers	$ 101,541	$ 5,812	$ 107,353
Bulk Sales to Haulers	-0-	1,750	1,750
Other Revenues:			
Forfeited Discounts	1,325		1,325
Service Discount	1,280		1,280
Connection Fees	3,725	<3,725>	-0-
Total Operating Revenue	$ 107,871	$ 3,837	$ 111,708

COMMENTARY

Parksville is a nonprofit water district, organized and existing under the laws of the Commonwealth of Kentucky and serves approximately 745 customers in Boyle County, Kentucky.

TEST PERIOD

Parksville proposed, and the Commission has accepted, the 12-month period ended May 31, 1983, as the test period for determining the reasonableness of the proposed rates. In utilizing the historic test period, the Commission has given full consideration to known and measurable changes found reasonable.

REVENUES AND EXPENSES

Parksville proposed several adjustments to its test-period revenue and expenses. The Commission, in its consideration of these proposed adjustments, has concluded that the following modifications will be necessary to determine a reasonable and acceptable level of test-period revenues and expenses for rate-making purposes:

Connection Fees

As indicated previously in this Order, connection fees in the amount of $3,725 were reported as revenue by Parksville on its test-period income and expense statement. According to the Uniform System of Accounts for Class C and D Water Utilities as prescribed by this Commission, such fees are to be recorded as contributions in aid of construction in Account No. 271.1--Tap-on Fees. Therefore, the Commission has both reduced Parksville's test-period operating revenues and increased its contributions in aid of construction by the $3,725 amount, thereby reflecting the proper classification of these fees. In addition, the Commission gives Parksville notice that all future connection fees collected by Parksville shall be recorded as contributions in aid of construction per the prescribed balance sheet account.

Purchased Water Expense

Based upon a comparison of actual monthly water purchases and average monthly water sales during the test period, Parksville estimated its unaccounted-for water to be 38 percent, which represented an excess of 23 percent above the Commission's allowable ratio of 15 percent. To reflect a purchased water expense that would include only the allowable amount of unaccounted-for water, Parksville proposed an adjustment to decrease test-period operating expenses by $13,280--an amount equivalent to the 23 percent excess of unaccounted-for water.

Based upon a comparison of the number of gallons of water purchased per the schedule of water purchases and sales, and the number of gallons of water sold per the revised billing analysis, the Commission has determined Parksville's unaccounted-for water to be 41.4 percent.[2] As this percentage far exceeds the acceptable unaccounted-for water ratio of 15 percent, the Commission has determined Parksville's maximum allowable water purchases to be 45,139,882 gallons. To these maximum allowable

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Total Gallons Purchased	65,516,803
Less: Total Gallons Sold	38,368,900
Unaccounted-for Water	27,147,903
Unaccounted-for Water Percentage	41.4%

water purchases the Commission has applied the rates currently being charged by Parksville's water supplier, the City of Danville, resulting in adjusted purchased water expense in the amount of $36,414. Therefore, to reflect the total allowable expense, the Commission has decreased Parksville's test-period operating expenses by $22,734.

Fuel or Power Purchased for Pumping

Parksville proposed an adjustment to increase its test-period operating expenses by $218 to reflect its electricity expense on an accrual rather than a cash basis. The Commission, in its examination of this expense item, has applied to Parksville's test-period electricity consumption data the rates currently being charged by Parksville's two electricity suppliers, Kentucky Utilities Company and Inter-County Rural Electric Cooperative Corporation, which results in a total allowable expense of $11,914, an increase of $950.

Operation and Maintenance Expense--Supplies and Equipment

According to its statement of operation and maintenance expenses, Parksville incurred test period supplies and equipment expense in the amount of $2,450. An examination of Parksville's cash disbursements journal revealed that this amount represented a single purchase from W. G. Feather and Son ("Feather and Son"), as referenced by Check No. 3342, dated October 12, 1983.[3] Although requested by the Commission, documentation was not provided in

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3 Cash Disbursement's Journal, October 1982, Response to Commission's Information Request dated January 10, 1984.

support of this expense item; however, Parksville stated that the amount represented the costs associated with the purchase of an emergency standby pump.[4] The Commission is of the opinion that this item, which represents an equipment purchase, should not be included as an expense on the income statement, but should be capitalized in the appropriate utility plant in service account. Therefore, the Commission has decreased Parksville's test-period operating expenses by $2,450 to reflect the exclusion of this amount as an expense for rate-making purposes. In addition, an adjustment has been made to increase Parksville's test-period depreciation expense by $123 to reflect the annual depreciation associated with the capitalized amount based on an estimated life of 20 years.

Transmission and Distribution Expenses--Operation Labor

Parksville proposed an adjustment to increase its test-period operating expenses by $2,426 to reflect salary increases granted to its operator and part-time laborers on June 30, 1983. Parksville stated in its application that the wage increases were necessary to bring the salaries of its employees up to minimal standards. In addition, Parksville indicated that its operator, John W. Feather, was paid a salary of $150 per week during the test period, whereas its part-time laborers were paid an hourly wage of $3.35 on an as-needed basis.[5]

4 Response to Commission's Information Request dated March 19, 1984, Item No. 2.

5 Response to Commission's Information Request dated January 10, 1984, Item No. 5.

The Commission, in consideration of this adjustment, has examined various aspects of Parksville's operations, including water line loss and compliance with Commission reporting requirements. With regard to these two particular areas, the Commission finds Parksville's 41.4 percent of unaccounted-for water to be excessive, with little apparent action having been taken to remedy this longstanding problem. Moreover, the Commission has concluded that Parksville's compliance with the Commission's reporting requirements remains haphazard at best, particularly with regard to its reporting of its monthly unaccounted-for water figures, as ordered by the Commission in Case No. 8365, An Adjustment of Rates of Parksville Water District.[6] Therefore, the Commission is of the opinion that the current status of the management of Parksville's operations does not merit a wage increase of this magnitude to be absorbed by Parksville's customers. In addition, due to the as-needed nature of the services provided by Parksville's part-time laborers, the Commission considers any proposed wage increases for these employees to be not sufficiently known and measurable. As a result of these findings, the Commission has not allowed Parksville's proposed adjustment to test-period operating expenses to reflect an increase in the amount of operational labor expense. However, in its examination of the salary currently being paid to Parksville's operator, the Commission has determined the allowable amount of this test period expense to be $7,800, based upon a

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6 Commission's Order in Case No. 8365 dated May 21, 1982.

salary of $150 per week for a period of 52 weeks. Therefore, the Commission has increased Parksville's test-period operating expenses by an amount of $450 to reflect the allowable amount of operational labor expenses.

Maintenance of Standpipes

Parksville proposed an adjustment to increase its test-period operating expenses in the amount of $3,000 to reflect the 6-year amortization of the total cost of painting its two water storage tanks. In its application, Parksville presented a price quotation from the Leary Construction Company, Inc., ("Leary") in which Leary proposed a plan whereby the outside of each storage tank would be painted every 6 years, and the inside would be painted every 3 years. The cost of painting both tanks was estimated to be $6,000, which, based on the maintenance plan proposed by Leary, results in a total cost of $18,000 over the 6-year period. Therefore, using this 6-year period as a basis, Parksville determined the proposed amount of test period amortization to be $3,000 on the $18,000 total amount.

The Commission, having recognized the importance and necessity of maintaining these tanks in order to insure a safe and adequate water supply for Parksville's customers, has allowed this $3,000 adjustment to Parksville's test-period operating expenses. However, in allowing this adjustment, the Commission hereby gives Parksville notice that the consideration of such proposed expenses in any future proceeding will be conditioned on Parksville's utilization of these allowable amounts for the purpose specified herein.

Maintenance of Mains

Parksville proposed an adjustment to increase its operating expenses in the amount of $4,450 to reflect the total amount of test-period expenses actually incurred in association with the maintenance of water mains. According to the application, the proposed adjustment represented expense items which had been incurred by Parksville, but, due to a lack of funds, had actually been paid by Feather and Son. Parksville requested the inclusion of this adjustment in the determination of its rates in an effort to generate a level of revenues that would enable it to reimburse the $4,450 amount to Feather and Son.

Parksville stated that its operations are reported on a modified accrual basis of accounting; therefore, these maintenance expense items were neither recorded as liabilities on its balance sheet, nor reported as expense on its income statement. In addition, although Feather and Son absorbed the cost associated with these items, no formal agreement was negotiated whereby Feather and Son was authorized to pay these amounts for Parksville. However, Parksville indicated that Mr. Bruce Feather, who is Parksville's manager and treasurer, had, on several occasions, assumed responsibility for Parksville's debts when Parksville experienced insufficient cash flow.[7]

In its application, Parksville submitted several invoices in documentation of the proposed $4,450 adjustment. Each of these

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7 Response to Commission's Information Request dated January 10, 1984, Item No. 8a.

invoices, which represented purchases from either Mid-State Meter and Supply Company, Inc., or Don Molden Pipe and Supply, were billed to Feather and Son, instead of Parksville. Parksville stated that the invoices were billed in this manner due to its lack of funds with which to pay the billed amounts.[8]

The Commission, in an examination of these invoices, has determined that the purchases associated with the various amounts represent items which should be capitalized in Parksville's utility plant in service accounts. Therefore, the Commission has disallowed the $4,450 proposed adjustment as an expense. However, the Commission has increased Parksville's test-period depreciation expense by $89 to reflect the amount of annual depreciation that would be associated with the capitalized amounts based on an estimated life of 50 years. The Commission also finds that any item of utility plant that may be purchased by Parksville in the future shall be properly recorded in its respective utility plant in service account, and shall be depreciated at an appropriate rate on the straight-line basis.

With regard to the arrangement that currently exists whereby Feather and Son is absorbing a portion of Parksville's operating expenses, the Commission gives Parksville notice that for consideration of such expenses in any future proceedings, Parksville shall supply verifiable authorization of each expense item, as well as adequate documentation and justification of the item's cost and necessity. In addition, all legitimate expenses shall be

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8 Ibid., Item No. 8c.

reported on Parksville's statement of income, and any liabilities incurred in association with these expenses shall be properly reported on Parksville's balance sheet, thereby complying with the reporting requirements established by the Uniform System of Accounts for Class C and D Water Utilities.

Maintenance of Meters

Parksville proposed an adjustment to increase its test-period operating expenses by $540 to reflect the costs associated with the installation of meters for 22 new customers. According to the application, this adjustment represents an amount that is owed to Feather and Son for the rental of equipment used to install the new meters. Documentation of this expense was submitted in the form of a bill from Feather and Son, which reflected the rental charges for what was termed a digging machine. The Commission, in its examination of this item, is of the opinion that as the $540 amount reflects charges associated with original meter installations, it does not constitute a test-period operating expense to Parksville. According to the Uniform System of Accounts for Class C and D Water Utilities, this amount should be capitalized in Account No. 347--Meter Installations. Therefore, the Commission has disallowed the $540 proposed adjustment. However, Parksville's depreciation expense has been increased by $11 to reflect the amount of annual depreciation that would be associated with the capitalized amount based on an estimated life of 50 years.

Accounting and Collecting Labor

Parksville proposed an adjustment to increase its test-period operating expenses in the amount of $1,300 to reflect a $25 per week salary increase which was granted to its billing and accounting clerk on June 30, 1983. During the test period, Parksville's clerk was paid a salary of $150 per week for the performance of duties which included preparing water bills, maintaining customer accounts and collecting funds. No additional duties or responsibilities were indicated as having been assigned to the accounting clerk in association with the proposed salary increase. However, as indicated in a previous section of this Order, Parksville stated that the proposed salary increases were granted in an effort to raise employees' wages to minimal standards.

In consideration of this proposed adjustment, the Commission has examined the necessity of the proposed salary increase on the basis of the duties and responsibilities of Parksville's accounting clerk, and has found that the proposed increase has not been adequately justified. Moreover, in consideration of the numerous inaccuracies revealed in Parksville's financial data, the Commission is of the opinion that the inconsistent quality of this information further substantiates the disallowance of this adjustment. Therefore, as the Commission finds that an increase in this salary area should not be absorbed by Parksville's customers, no adjustment has been made to increase test-period accounting and collecting labor expenses.

Administrative and General Salaries

Parksville proposed an adjustment to increase operating expenses by an amount of $2,400 to reflect the payment of a $50 per month fee to each of its three commissioners, as well as an increase in the manager's salary by an amount of $50 per month. With regard to the proposed commissioners' fees, Parksville stated that no payments had been made to or benefits received by these persons previously, and that the proposed increase was requested in the rate schedule for future salary payments if the funds become available.[9] In addition, Parksville indicated that the $50 per month salary increase to its manager was granted by its commissioners on June 10, 1983.

In consideration of Parksville's current financial status, the Commission seriously questions the payment of a monthly fee to Parksville's three commissioners, as well as an increase in salary to its manager. The Commission disallowed a similar adjustment for Parksville in its last general rate case and indicated that such an adjustment was inappropriate due to deficiencies in Parksville's operations. The Commission has found little evidence to indicate any constructive action having been taken by Parksville to improve its management and operations since Parksville's last rate case. For instance, Parksville's unaccounted-for water remains excessive, having actually increased to a level of 41.4 percent subsequent to its previous rate adjustment case. In addition, Parksville's accounting records contain many questionable

9 Ibid., Item No. 6.

items, and in several areas do not comply with the Uniform System of Accounts for Class C and D Water Utilities. Finally, Parksville's responses to several of the items requested during the course of these proceedings have been vague, resulting in information that is of minimal use to the Commission in rendering a decision in this case. In light of these factors, the Commission is of the opinion that Parksville has not adequately justified the payment of fees to its commissioners or an increase in salary to its manager, and has, therefore, disallowed the proposed $2,400 adjustment to increase administrative and general salaries.

Outside Services Employed

Parksville proposed an adjustment to increase its test-period operating expenses in the amount of $3,558 to reflect the costs associated with the services of an accounting firm, the retention of legal counsel, and the preparation of the rate adjustment application. Parksville submitted a quotation from Critchfield and Critchfield, Certified Public Accountants, wherein the firm stated that it would, for an annual fee of $1,650 conduct a monthly review of Parksville's journals and records, prepare monthly financial statements, and prepare the annual report to the Commission. According to the application, Parksville is presently incurring an annual cost of $275 in association with limited accounting services; therefore, to reflect the $1,650 amount, an adjustment was proposed to increase outside services expenses in the amount of $1,375.

As a result of the examination of the financial information presented in this proceeding, the Commission is of the opinion that Parksville would benefit substantially from professional accounting services in areas such as the compilation, review and preparation of financial statements. Moreover, the Commission finds that the quality of Parksville's financial information is in many respects inadequate and untimely and, therefore, is a major contributing factor in the management inefficiencies that Parksville is currently experiencing. In consideration of these factors, the Commission has allowed the proposed adjustment to increase outside services in the amount of $1,375 to reflect the costs associated with the contracting of professional accounting services. However, the Commission notifies Parksville that in allowing this item, all future filings of financial information with the Commission will be closely scrutinized as to the accuracy thereof, and such information will be monitored with regard to its conformity with the procedures and requirements established by the Uniform System of Accounts for Class C and D Water Utilities.

Also included in the $3,558 proposed adjustment to outside services was an amount of $900 which reflected the anticipated costs associated with the retention of legal counsel. Parksville indicated that it presently does not incur any attorney fees, as such services are currently being provided at no charge. However, according to the application, Parksville's commissioners voted to retain at a fee of $75 per month the attorney who is presently providing these services.

Parksville stated that the attorney would be retained to advise the commissioners as needed and to prepare legal documents such as contracts, right of way agreements, and deeds.[10] However, Parksville did not present either a finalized contract or a price quotation which indicated the specific legal services to be provided for the retainer. On the basis of the information presented in support of this adjustment, the Commission is of the opinion that Parksville has not adequately represented the necessity of its retaining legal counsel. Therefore, the Commission has disallowed the proposed $900 adjustment to outside services.

The remainder of Parksville's proposed $3,558 adjustment to outside services was comprised of a $1,283 amount which represented the first year of a 3-year amortization of the $3,850 fee which was negotiated with BADD for its preparation of the rate adjustment application. In support of this expense, Parksville submitted as a part of its application a finalized contract between Parksville and BADD which specified the various terms and conditions whereby BADD would prepare the application. To further document the $3,850 amount, the Commission requested that Parksville provide a detailed breakdown of its rate case expense, reflecting a description of the specific services provided, the number of hours associated with each service, and the hourly rate charged per each service. In response, Parksville submitted a breakdown classified on the basis of a fee charged per the number of "man-days" expended by each of the four staff members of BADD who were involved in the preparation of the application. This

10 Ibid., Item No. 9.

breakdown reflected a total rate case expense of $2,751 as having been incurred.[11]

The ARF procedure was established as a simplified and less expensive method in which small utilities could file for rate adjustments. The Commission is of the opinion that the expenses associated with rate adjustment applications filed under this procedure should be limited to a maximum of $1,000, to be amortized over a period of 3 years, unless justification for additional cost has been provided. The Commission has reviewed the application and record in this matter, and finds the $3,850 fee to be excessive for an ARF proceeding, particularly in consideration of the limited usefulness of a substantial portion of the information presented in this case. The Commission has examined the breakdown of the services provided by BADD and finds many of the services provided by the various personnel of BADD to be repetitious, particularly in the areas of billing and consumption analysis and rate analysis. In addition, the Commission is of the opinion that the amount of time expended in the preparation of certain areas of the application is excessive, as tasks such as the development of a billing analysis, financial exhibit and rate schedule can be accurately accomplished in a much less substantial time period. The Commission is also aware that due to the varying quality of the available financial information, the amount of work involved in some areas of this case exceeded that which is normally encountered in an ARF proceeding. However, in many

[11] Ibid., Item No. 10.

instances the information submitted by Parksville was vague, incomplete, or not presented in the requested form.

In determining the allowable level of rate case expense, the Commission has examined the breakdown submitted by Parksville and has concluded that the information contained therein does not clearly reflect the amount of expense incurred per the specific services provided as requested by the Commission. Moreover, as indicated in other sections of this Order, the quality of financial information submitted by Parksville has been found to be inaccurate and inconsistent in many instances. The Commission is of the opinion that to represent the costs associated with the amount of usable information as originally presented by Parksville, only 60 percent of the actual rate case expense should be allowed for rate-making purposes to be amortized over a period of 3 years. Therefore, Parksville's test-period operating expenses have been increased by $550 to reflect the test period amortization of the allowable regulatory commission expense of $1,650.

Miscellaneous General Expense

The statement of income and expenses submitted by Parksville reflected miscellaneous general expenses in the amount of $1,951 as having been incurred during the test period. An examination of Parksville's cash disbursements journal revealed that of this amount total payments of $1,615 were made to Feather and Son during the test period. These payments included $1,140 which Parksville indicated was associated with rent, telephone and electricity expenses. Of the additional $475 in payments to

Feather and Son, Parksville indicated that an amount of $250 represented payments for expenses incurred prior to the test period; however, no documentation or verification was offered as to the nature of the remaining payments in the amount of $225. The Commission is of the opinion that the allowance of expense items not incurred during the test period violates the concept of revenue and expense matching. In addition, the Commission finds that Parksville's ratepayers should not be required to absorb expenses that are not documented, verified, or adequately explained as to the nature thereof. Therefore, the Commission has decreased Parksville's operating expenses in the amount of $475 to reflect the allowable miscellaneous general expense in the amount of $1,476.

Transportation Expenses

According to the test-period statement of income and expenses, Parksville incurred transportation expenses in the amount of $6,882. An examination of Parksville's cash disbursements journal revealed that of this amount, $6,464 represented payments to Feather and Son. Parksville stated that this amount was reflective of a $10 per day truck lease fee, as well as $3.60 per day for gasoline. In addition, the remainder of the total expense represented payments to other parties in the amount of $348 for gasoline and $70 for truck repair parts.[12]

[12] Response to Commission's Information Request dated March 21, 1984, Item No. 1.

No documentation was submitted by Parksville in support of these amounts, although such verification was requested by the Commission.[13] However, Parksville did indicate that the payments to Feather and Son were approved by Parksville's board of commissioners on January 21, 1982.[14]

The Commission, in its consideration of this expense, has concluded that the payment of a flat-rate lease fee and a gasoline charge to Feather and Son is not indicative of a true measure of Parksville's transportation expense. The Commission is of the opinion that such expenses should be based upon a standard rate applied to the number of miles the vehicle is driven in association with district business. Moreover, the Commission seriously questions the particular arrangement that exists between Parksville and Feather and Son with regard to these payments, as such payments do not seem to constitute arms-length transactions due to the fact that Mr. Bruce Feather, being treasurer of Parksville, is responsible for the disbursement of funds to pay such expenses.

With regard to these amounts, the Commission finds that Parksville has not adequately substantiated its test-period transportation expenses, as no supporting invoices, bills, or cancelled checks were provided to document these payments. Therefore, for the purposes of determining rates in this case, the Commission has disallowed the entire $6,882 amount of test-period transportation expenses. In addition, the Commission hereby notifies Parksville

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13 Ibid.

14 Ibid., Item No. 3.

that without proper verification or documentation as requested by this Commission, such expenses will not be allowed in any future rate adjustment proceedings.

Sales Tax

On its test-period statement of income and expenses, Parksville reported sales tax expense of $139. The Commission is of the opinion that in collecting these taxes, Parksville is merely an agent of the taxing authority, and, as such, should not report any expense in association with these collections. Only in those situations in which a residual or commission is paid by the taxing authority for the collection services of the agent would any amount be reported. Therefore, the Commission has decreased Parksville's test-period operating expenses by $139 to exclude sales tax.

Taxes Other Than Income or Sales

Parksville proposed a $2,215 adjustment to increase operating expenses to reflect social security contributions of $1,608, as well as workman's compensation premiums of $607 based upon Parksville's proposed wages and salaries. The Commission, in its consideration of these adjustments, recognizes the fact that these expenses represent withholdings and payments that are required by federal and state regulations, and finds that such expenses should be included in the establishment of Parksville's rates. However, the Commission has determined the amount of these expenses on the basis of the wages and salaries allowed herein.

In its calculation of Parksville's social security taxes, the Commission has applied the 1984 withholding rate of 7 percent[15] to the total allowable wages and salaries of $15,511, resulting in an allowable expense of $1,086.[16] With regard to the allowable amount of workman's compensation premiums, the Commission has determined its adjustment to this expense on the basis of the cost of the insurance premium proposed by Parksville expressed as a percentage of Parksville's proposed wages and salaries of $24,000. This calculation results in a test-period workman's compensation premium of $392.[17] Therefore, the Commission has increased Parksville's test-period operating expenses by $1,478 to reflect the total allowable amount of these expenses.

Interest on Notes Payable

Parksville proposed an adjustment to decrease its test-period operating expenses in the amount of $864 to reflect the

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15 Federal Tax Guide, paragraph 17,506, Commerce Clearing House.

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Allowable test period wages:	
Operational labor	$ 7,800
Meter reading labor	721
Accounting and collecting labor	6,140
Administrative salaries	850
Total allowable wages	$15,511
FICA rate as of 1/1/84	7%
Allowable social security taxes	$ 1,086

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Total allowable wages	$15,511
Premium rate: ($500 ÷ $24,000)	.0208
Allowable premium amount	$ 323
Kentucky tax and assessment at 21.31 percent	69
Total allowable expense amount	$ 392

amount of interest associated with the outstanding balance of notes payable at the end of the test period. In proposing this adjustment, Parksville indicated that its $3,614 of test-period interest expense was accrued at a rate of 10 percent per annum on three notes payable to Farmers Bank of Danville, Kentucky, ("Farmers Bank") in the total amount of $27,500. In addition, Parksville stated that these notes were utilized to offset operating deficits attributed to negative cash flow.[18]

The Commission in determining Parksville's rates in Case No. 8365 allowed a 1.2X debt service coverage ratio, thereby providing sufficient revenues to meet its principal and interest payments on all outstanding debt. Moreover, in Case No. 8365, the Commission concluded that the rates established therein would produce a level of revenue sufficient to pay its operating expenses.[19]

As Parksville has indicated that funds from the three notes payable to Farmers Bank were utilized to pay operating expenses, and as rates have previously been established which would adequately provide for payment of such expenses, the Commission is of the opinion that, in determining Parksville's rates in this case, the allowance of interest expense on these notes would constitute retroactive rate-making. Therefore, the Commission has

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18 Response to Commission's Information Request dated January 10, 1984, Item No. 12.

19 Commission's Order in Case No. 8365 dated May 21, 1982.

disallowed Parksville's test-period interest expense on notes payable in the total amount of $3,614.

Depreciation Expense

Parksville reported on its test-period income and expense statement depreciation expense of $7,197, which was determined on the basis of the amount of depreciation expense allowed by the Commission in Case No. 8365. However, actual depreciation on plant in service at the end of the test period was $7,435.

The Commission, in its analysis of this expense, determined Parksville's total utility plant in service to be $378,705 based upon the balance of utility plant at the end of the test period adjusted for the items to be capitalized as determined herein.[20] In addition, Parksville's contributions in aid of construction account was adjusted herein to reflect the $3,725 of connection fees erroneously reported as revenue, thereby resulting in total adjusted contributions in aid of construction of $15,642.[21] This amount was deducted from the total adjusted balance of utility plant in service, which resulted in net utility plant in service

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Utility plant in service as of 5/31/83	$368,765
Add: Items to be capitalized:	
Standby pump	2,450
Copier	2,500
Meter installation	540
Amount from maintenance of mains	4,450
Adjusted utility plant in service	$378,705

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Test-year-end contributions	$11,917
Connection fees reported as revenue	3,725
Adjusted test period contributions	$15,642

of \$363,063.[22] A composite depreciation rate of 2.24 percent,[23] based upon the ratio of adjusted test-period depreciation expense to the balance of utility property as determined herein, was applied to the \$363,063, which resulted in an allowable depreciation expense of \$8,133. Therefore, to reflect this allowable amount, the Commission has increased Parksville's actual test-period depreciation expense by \$697.

Interest on Long-Term Debt

Parksville proposed an adjustment to increase test-period operating expenses by \$13,899 to reflect the amount of principal requirements associated with its 1965 and 1966 bond issues. As debt service coverage is the major factor considered in determining the revenue requirements of Parksville, the Commission is of the opinion that the principal requirements on these two bond issues should not be allowed as a pro forma adjustment to test-period operating expenses. The Commission has determined Parksville's allowable interest on long-term debt to be \$13,000,

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Adjusted utility plant in service	\$378,705
Less: adjusted contributions	15,642
Net utility plant in service	\$363,063

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Actual test-period depreciation expense		\$ 7,435
Adjustments:		
Copies	\$2,450 for 3 years	834
Standby pump	\$2,500 for 20 years	123
Mains	\$4,450 for 50 years	89
Meter installation	\$ 540 for 50 years	11
Adjusted test-period depreciation		\$ 8,492
Adjusted utility plant in service		÷378,705
Composite depreciation rate		2.24%

based upon the outstanding principal balances of Parksville's two bond issues at the end of the test period. Therefore, Parksville's test-period operating expenses have been decreased by $3,000, to reflect this allowable interest expense.

After consideration of the aforementioned adjustments, the Commission finds Parksville's test period operations to be as follows:

	Actual Test Period	Pro Forma Adjustment	Adjusted Test Period
Operating Revenues	$ 107,871	$ 3,837	$111,708
Operating Expenses	119,248	<30,296>	88,952
Net Operating Income	$ <11,377>	$ 34,133	$ 22,756
Interest Income	173		173
Interest on Long-Term Debt	16,000	<3,000>	13,000
Net Income	$ <27,204>	$ 37,133	$ 9,929

REVENUE REQUIREMENTS

Parksville indicated that its test-period revenue requirements were based on a calculation of cash flow relative to its pro forma adjusted expenses and the principal payments on its outstanding debt.[24] Having considered the information submitted in this proceeding, the Commission finds that the debt-service coverage method of revenue determination is the appropriate method to be utilized in calculating Parksville's test-period revenue requirements.

24 Response to Commission Information Request dated January 10, 1984, Item No. 15.

Parksville's long-term debt is composed of a 1965 bond issue with an outstanding principal balance of $210,000, and a 1966 bond issue with an outstanding principal balance of $47,000. Both of these bond issues accrue interest on the principal at a rate of 5 percent per annum. The 1966 bond issue requires annual repayments of principal, whereas the outstanding balance of the 1965 bond issue is to be repaid with a single balloon payment of $210,000 in 1995.

With regard to the 1965 bond issue, Parksville stated that in order to fund the 1995 balloon principal payment, an amount of $10,899 would be required to be deposited annually in a bond reduction account at a rate of 8.25 percent. The Commission is of the opinion that the 8.25 percent interest rate is a reasonable projection, and therefore, finds the $10,899 annual deposit amount to be an adequate estimation of Parksville's bond reduction fund requirements. As this amount has been included in Parksville's debt-service coverage calculations, the Commission also finds that Parksville should make the required annual deposit to the bond reduction fund in accordance with the terms and conditions of the 1965 bond ordinance.

The Commission finds that a 1.2X debt-service coverage factor is the appropriate coverage factor, and has applied this amount to a 5-year average of the principal and interest payments on Parksville's 1966 bond issue, as well as the fund requirements and interest on the 1965 bond issue. The resulting amount of $32,218, combined with Parksville's allowable test-period operating expenses of $88,952, produces a test-period revenue requirement of $121,170.

The Commission, in determining a revenue requirement on which to base Parksville's water rates, has made several adjustments to Parksville's actual and proposed test period expenses. In addition, many items were adjusted or disallowed on the basis of inadequate justification or lack of verification and documentation of expense amounts. As the information upon which a rate decision is based must conform with known and measurable standards, the Commission notifies Parksville that for consideration in any future rate adjustment proceedings, all information must be adequately documented, verified, and justified, and must be submitted in accordance with the requirements as set forth by this Commission.

In addition, the Commission is very much concerned about the current status of Parksville's operations. Parksville has shown little, if any, improvement in areas such as the control of unaccounted-for water, the maintenance of accurate and timely information, and the conformance with the Commission's filing and reporting requirements. These operational deficiencies cannot be rectified through continuous rate increases, but must be corrected by efforts of management to improve the physical as well as financial aspects of Parksville's operations based on recommendations of the Commission in this and previous Orders. The Commission urges Parksville to take immediate corrective action to remedy these management inefficiencies, thereby insuring proper operation of the district and adequate water service to its customers.

SUMMARY

The Commission, having considered the evidence of record and being advised, is of the opinion and finds that:

1. The rates in Appendix A are the fair, just and reasonable rates to be charged by Parksville, as they will produce annual revenues in the amount of $118,392. This revenue, along with other income in the amount of $2,778, will be sufficient to meet Parksville's operating expenses found reasonable for rate-making purposes, service its debt and provide a reasonable surplus.

2. The rates proposed by Parksville would produce revenue in excess of that found reasonable herein and should be denied.

3. Parksville's accounting records are not in compliance with the reporting requirements established by the Uniform System of Accounts for Class C and D Water Utilities, as its results of operations are not reported in accordance with the accrual basis of accounting.

4. Parksville's unaccounted-for water remains excessive, and, as a result, Parksville should continue to file monthly reports on its unaccounted-for water until an amount of 15 percent or less is attained over a period of 3 consecutive months.

5. This case has revealed the existence of serious problems with regard to Parksville's management and operations.

Therefore, an informal conference should be scheduled between the Commission and Parksville's commissioners and management to discuss these problem areas.

IT IS THEREFORE ORDERED that the rates in Appendix A be and they hereby are approved for service rendered by Parksville on and after the date of this Order.

IT IS FURTHER ORDERED that the rates proposed by Parksville be and they hereby are denied.

IT IS FURTHER ORDERED that Parksville shall maintain its accounting records in compliance with requirements established by the Uniform System of Accounts for Class C and D Water Utilities, and shall report the results of its operations in accordance with the accrual basis of accounting.

IT IS FURTHER ORDERED that Parksville shall continue to file monthly reports regarding the level of its unaccounted-for water until an amount of 15 percent or less is attained for a period of 3 consecutive months.

IT IS FURTHER ORDERED that Parksville shall file a statement in its annual report for each year through December 31, 1995, detailing its compliance with the bond fund provisions of its 1965 bond ordinance and specifying the total amount of annual deposits into the required account.

IT IS FURTHER ORDERED that an informal conference shall be scheduled between the Commission and Parksville's commissioners and management to discuss the problem areas that exist in Parksville's operations.

IT IS FURTHER ORDERED that, within 30 days of the date of this Order, Parksville shall file its revised tariff sheets setting forth the rates approved herein.

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

PUBLIC SERVICE COMMISSION

Chairman

Vice Chairman

Commissioner

ATTEST:

Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE COMMISSION IN CASE NO. 8907 DATED 6/26/84

The following rates are prescribed for the customers served by the Parksville Water District. 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.

RATES

Gallonage Blocks	Monthly Rate
First 1,000 gallons	$6.80 (minimum 5/8" meter)
Next 4,000 gallons	2.00 per 1,000 gallons
Next 5,000 gallons	1.85 per 1,000 gallons
Over 10,000 gallons	1.70 per 1,000 gallons

The minimum monthly bill for 1-inch meters shall be $14.80 for which the user will be entitled to 5,000 gallons of water. Usage in excess of 5,000 gallons per month shall be billed the same as all other customers.

Bulk Sales

All Usage	$3.50 per 1,000 gallons