

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF SOUTH GRAVES COUNTY )  
WATER DISTRICT FOR (1) A CERTIFICATE )  
OF CONVENIENCE AND NECESSITY; (2) )  
AUTHORIZATION TO BORROW FUNDS AND TO ) CASE NO. 94-004  
ISSUE ITS EVIDENCE OF INDEBTEDNESS )  
THEREFOR; AND (3) FOR AUTHORITY TO )  
ADJUST RATES )

O R D E R

On February 2, 1994, South Graves County Water District ("South Graves") filed its application for Commission approval of proposed water rates. Commission Staff, having performed a limited financial review of South Graves' operations, has prepared the attached Staff Report containing Staff's findings and recommendations regarding the proposed rates. All parties should review the report carefully and provide any written comments or requests for a hearing or informal conference no later than 15 days from the date of this Order.

IT IS THEREFORE ORDERED that all parties shall have no more than 15 days from the date of this Order to provide written comments regarding the attached Staff Report or requests for a hearing or informal conference. If no request for a hearing or informal conference is received, this case will be submitted to the Commission for a decision.

Done at Frankfort, Kentucky, this 18th day of April, 1994.

ATTEST:

D. Mills  
Executive Director

PUBLIC SERVICE COMMISSION

G. L. DeLoach  
For the Commission

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF SOUTH GRAVES COUNTY )  
WATER DISTRICT FOR (1) A CERTIFICATE )  
OF CONVENIENCE AND NECESSITY; (2) )  
AUTHORIZATION TO BORROW FUNDS AND TO ) CASE NO. 94-004  
ISSUE ITS EVIDENCE OF INDEBTEDNESS )  
THEREFOR; AND (3) FOR AUTHORITY TO )  
ADJUST RATES )

STAFF REPORT

Prepared By: Jack Scott Lawless, CPA  
Public Utility Financial  
Analyst  
Water and Sewer Revenue  
Requirements Branch  
Division of Financial Analysis

Prepared By: John Geoghegan  
Public Utility Rate  
Analyst  
Communications, Water  
and Sewer Rate Design Branch  
Rates and Research Division

STAFF REPORT

ON

SOUTH GRAVES WATER DISTRICT

CASE NO. 94-004

A. Preface

On February 2, 1994, South Graves Water District ("South Graves") filed its application with the Kentucky Public Service Commission ("Commission") seeking approval to increase its tariffed rates by 120.42 percent, an increase in annual operating revenues of \$165,210.

In order to evaluate the requested increase, the Commission Staff ("Staff") chose to perform a limited financial review of South Graves' operations for the test period, the twelve month period ending August 31, 1993. Jack Scott Lawless, of the Commission's Financial Analysis Division, conducted the review at South Graves' office in Wingo, Kentucky. John Geoghegan, of the Commission's Rates and Research Division, performed his review at the offices of the Commission in Frankfort, Kentucky.

The findings of the field review have been reduced to writing in this report. Mr. Geoghegan is responsible for the sections related to operating revenues and rate design. The remaining sections of this report were prepared by Mr. Lawless. Based upon the findings of this report, Staff recommends that South Graves be allowed to increase its normalized operating revenues by 113.15 percent, an increase in annual operating revenues of \$157,521.

Scope

The scope of the review was limited to obtaining information to determine whether test period operating revenues and expenses were

representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

During the course of the review, South Graves was advised that all proposed adjustments to test year expenses must be supported by some form of documentation and that all such adjustments must be known and measurable as well as reasonable.

B. Analysis of Operating Revenues and Expenses

Operating Revenue

South Graves provided a billing analysis in its application for the test year showing revenue from water sales of \$139,218. Exhibit F of the application, Monthly Operating Revenues and Expenses, showed a total of \$137,196 in revenue from water sales, an adjustment of \$2,022.

Operating Expenses

South Graves reported operating expenses of \$122,485 for the test year which it proposed to increase by \$28,617. Staff has adjusted test year operating expenses in the amount of \$10,466. South Graves' and Staff's adjustments are discussed in the following sections of this report. Staff's adjustments are shown on Appendix B attached to this report.

Source of Supply

Staff has reduced source of supply expenses by \$1,133<sup>1</sup> to reflect the 3 year amortization of test year tank repair. During the test year South Graves paid \$1,700 to repair a leak in a water tower. This item is an operating expense that will benefit South Graves for more than one period and is nonrecurring in nature. Therefore, Staff recommends that the cost of the repair be amortized over three years.

Staff has also decreased source of supply expenses by \$1,340<sup>2</sup> in order to eliminate test year purchases which should have been capitalized. The appropriate recovery will be allowed in Staff's depreciation adjustment.

Administrative and General

South Graves proposed to increase test year administrative and general expenses by \$1,632 to recover the proposed KIA loan servicing fee. Staff agrees with this adjustment and has included it in its revenue requirements determination.

|              |                       |                   |
|--------------|-----------------------|-------------------|
| <sup>1</sup> | Cost of repair        | \$ 1,700          |
|              | Amortize over 3 years | <u>3</u>          |
|              | Annual recovery       | 567               |
|              | Less: Test year       | <u>(1,700)</u>    |
|              | Adjustment            | <u>\$ (1,133)</u> |
| <sup>2</sup> | Cost of Pump          | \$ (840)          |
|              | Cost of Land          | <u>(500)</u>      |
|              | Adjustment            | <u>\$ (1,340)</u> |

Salaries and Wages

South Graves allocated test year salaries and wages of \$38,392 to its operation and maintenance expense accounts. Staff has decreased this amount by \$8,376<sup>3</sup> to reflect South Graves' employees and their pay rates as of the date of Staff's field review.

Taxes Other Than Income Taxes

The 'taxes other than income taxes expense' account has been adjusted in conjunction with the salaries and wages adjustment. This results in a decrease of \$641<sup>4</sup>.

Rate Case Amortization

South Graves proposed a rate case expense amortization adjustment in the amount of \$3,500. However, the cost of the rate case has been included in the proposed construction project financing as shown on Page 3 of Petitioner's Exhibit L. Therefore, this adjustment has been eliminated to prevent double recovery of the expense.

Loss on Disposal of Asset

South Graves proposed to include as a revenue requirement a \$4,123 loss on the disposal of an asset. It is Staff's position that this loss is a one-time, nonrecurring event. Since rates are set prospectively, this adjustment should not be included in the revenue requirement

---

|              |                              |                   |
|--------------|------------------------------|-------------------|
| <sup>3</sup> | Pro forma Salaries and Wages | \$ 30,016         |
|              | Less: Test year              | <u>(38,392)</u>   |
|              | Adjustment                   | <u>\$ (8,376)</u> |
| <sup>4</sup> | Salary adjustment            | \$ 8,376          |
|              | Times: FICA tax rate         | <u>7.65%</u>      |
|              | Adjustment                   | <u>\$ (641)</u>   |

determination and has not been incorporated into the recommended revenue requirement.

Depreciation

South Graves proposed to increase test year depreciation expense by \$19,362 as a result of the proposed construction in this case. Staff agrees with this adjustment and has incorporated it in its determination of pro forma revenue requirements.

Staff has also adjusted test year depreciation to allow the cost recovery of the pump that was eliminated from operating expenses in a previous adjustment and to allow recovery for a post test period purchase of a computer for \$5,894. The resulting adjustment reflects the 7 year depreciable lives of these assets and is an increase to test year depreciation expense of \$962.

C. Revenue Requirements Determination

The approach frequently used by this Commission to determine revenue requirements for water districts with outstanding bond issuances such as South Graves, is a 120 percent debt service coverage on the average annual debt service payment. By utilizing this approach, Staff has calculated an increase in normalized operating revenues of \$157,521.

|                             |                        |
|-----------------------------|------------------------|
| Adjusted Operating Expenses | \$132,951 <sup>5</sup> |
| Average Annual Debt Service | 140,437 <sup>6</sup>   |

---

<sup>5</sup> See Appendix B

<sup>6</sup> Annual Principal and Interest Payments:

|                             |                   |
|-----------------------------|-------------------|
| 1995                        | \$ 139,968        |
| 1996                        | 140,803           |
| 1997                        | <u>140,538</u>    |
| Average Annual Debt Service | <u>\$ 140,437</u> |

|                                    |                           |
|------------------------------------|---------------------------|
| 20 Percent DSC                     | <u>28,087<sup>7</sup></u> |
| Total Revenue Requirement          | 301,475                   |
| Less: Normalized Operating Revenue | <u>(143,954)</u>          |
| Required Increase                  | <u>\$157,521</u>          |

In its revised calculation of its debt service revenue requirement, South Graves included a delinquent FmHA note payment which was due January, 1994, and a 2 year loan for the purchase of a computer in the amounts of, \$17,621 and \$2,500, respectively. After discussing these issues with South Graves' office manager, Staff discovered that the delinquent FmHA payment is being paid at a rate of \$4,000 per month and that the loan for the computer purchase was for only 1 year. Both of these debts will be fully paid before the rates in this case become effective. Therefore, Staff has not included either of these debts in its revenue requirement determination.

#### D. Rate Design

South Graves' present rate design includes metered customers on declining block rates, non-metered customers on flat monthly rates, and one contract customer on a flat monthly rate. However, its proposed rate design will place all customers on a uniform declining block rate design. Staff concludes that South Graves' proposed rate design will simplify its billing system and be more equitable to its customers.

The rates set out in Appendix A will produce \$296,739 in annual revenue from water sales.

---

|  |                  |
|--|------------------|
| <sup>7</sup> Average annual Debt Service | \$ 140,437       |
| Times: Debt Service Coverage Rate        | <u>20%</u>       |
| Debt Service Coverage (DSC)              | <u>\$ 28,087</u> |

E. Signatures

  
Prepared By: Jack Scott Lawless, CPA  
Public Utility Financial  
Analyst  
Water and Sewer Revenue  
Requirements Branch  
Rates and Tariffs Division

  
Prepared By: John Geoghegan  
Public Utility Rate  
Analyst  
Communications, Water and  
Sewer Rate Design Branch  
Research Division

## Appendix A

### South Graves County Water District

The following rates are recommended for South Graves County Water District.

#### Monthly Rates

|                      |                        |
|----------------------|------------------------|
| First 2,000 gallons  | \$14.25 (Minimum Bill) |
| Next 3,000 gallons   | 6.87 per 1,000 gallons |
| Next 5,000 gallons   | 6.62 per 1,000 gallons |
| Next 10,000 gallons  | 6.38 per 1,000 gallons |
| Next 30,000 gallons  | 5.89 per 1,000 gallons |
| Next 50,000 gallons  | 4.91 per 1,000 gallons |
| Over 100,000 gallons | 3.43 per 1,000 gallons |

APPENDIX B  
TO STAFF REPORT CASE 94-004

South Graves Water District  
Statement of Adjusted Operations

|                                  | Test<br>Year    | Adjustments        | Pro forma<br>Present<br>Rates |
|----------------------------------|-----------------|--------------------|-------------------------------|
| <b>Operating Revenues</b>        |                 |                    |                               |
| Water Sales                      | \$137,196       | \$2,022            | \$139,218                     |
| Forfeited Discounts              | 3,142           |                    | 3,142                         |
| Miscellaneous                    | 1,594           |                    | 1,594                         |
| <b>Total Operating Revenues</b>  | <b>141,932</b>  | <b>2,022</b>       | <b>143,954</b>                |
| <b>Operating Expenses</b>        |                 |                    |                               |
| <b>Operation and Maintenance</b> |                 |                    |                               |
| Source of Supply                 | 5,658           | (1,133)<br>(1,340) | 3,185                         |
| Pumping                          | 13,928          |                    | 13,928                        |
| Water Treatment                  | 10,886          |                    | 10,886                        |
| Trans. and Dist.                 | 32,217          |                    | 32,217                        |
| Customer Accounts                | 14,087          |                    | 14,087                        |
| Adm. and Gen.                    | 25,614          | 1,632              | 27,246                        |
| Salaries and Wages               |                 | (8,376)            | (8,376)                       |
| Other Taxes                      |                 | (641)              | (641)                         |
| <b>Total O &amp; M</b>           | <b>102,390</b>  | <b>(9,858)</b>     | <b>92,532</b>                 |
| Depreciation                     | 20,095          | 20,324             | 40,419                        |
| <b>Total Operating Expenses</b>  | <b>122,485</b>  | <b>10,466</b>      | <b>132,951</b>                |
| <b>Net Operating Income</b>      | <b>\$19,447</b> | <b>(\$8,444)</b>   | <b>\$11,003</b>               |