

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF HARDEMAN WATER)
DISTRICT FOR AN ADJUSTMENT OF)
RATES PURSUANT TO THE ALTERNATIVE) CASE NO. 2003-00107
RATE FILING PROCEDURE FOR SMALL)
UTILITIES)

O R D E R

On March 24, 2003, Hardeman Water District (Hardeman) filed its application for Commission approval of its proposed water rates. Commission Staff, having performed a limited financial review of Hardeman's 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 10 days from the date of this Order.

IT IS THEREFORE ORDERED that all parties shall have no more than 10 days from the date of this Order to provide written comments regarding the attached Staff Report or requests for 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 5th day of May, 2003.

By the Commission

ATTEST:


Executive Director

STAFF REPORT
ON
HARDEMAN WATER DISTRICT
CASE NO. 2003-00107

Pursuant to a request by Hardeman Water District (Hardeman) for assistance with the preparation of a rate application for its water operations, Commission Staff (Staff) performed a limited financial review of Hardeman s test year operations for the calendar year ending December 31, 2001. The scope of Staff s review was limited to obtaining information as to whether the test period operating revenues and expenses were representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

Upon completion of the review, Staff assisted Hardeman in the development and preparation of a rate application. The application included an adjusted pro forma operating income statement wherein adjustments were made to test year operating revenues and expenses that were known and measurable and deemed to be reasonable. The rates proposed by Hardeman were based on the pro forma income statement as shown in the application. The application also includes the calculation of Hardeman s revenue requirement using an operating ratio method, which is frequently used by the Commission to determine revenue requirements for small water utilities with little or no long-term debt. To generate the revenue requirement of \$101,467, Hardeman is proposing to increase its annual revenue from water rates by \$30,707, an increase of 43.39% over normalized revenue of \$70,760.

The 43% rate increase proposed by Hardeman is large in percentage terms, but several factors are worth noting. First, Commission records indicate that Hardeman last filed for a general rate increase in August of 1990, or more than 12 years ago. Since that time, Hardeman's costs have increased consistent with cost increases in the overall economy, including the cost of labor, materials, and other expenses.

Secondly, Commission records also indicate that Hardeman was one of 27 water utilities whose financial conditions were investigated by the Commission in 1997 and 1998. Those utilities were selected based upon a recurring pattern of net losses for the period from 1992 through 1996, suggesting the possible need for additional revenues. During the course of the Commission's investigation, Hardeman filed an annual report for 1997 which indicated that it had achieved a small net income for that year. Hardeman also indicated to the Commission that it was not interested in pursuing a rate increase at that time. Therefore, Hardeman has been very conservative in its approach to rate increases, even when prompted by the Commission to consider them.

Third, Hardeman's avoidance of rate increases over the years has resulted in its customers paying very affordable bills. For an average customer using 5,000 gallons, Hardeman's current rates would produce an average bill of \$14.80 per month, much lower than that of most water utilities regulated by the Commission.

Fourth, during the Staff's review, Hardeman indicated that it was facing the possibility of costly repairs to its 50,000 gallon elevated storage tank. Those repairs were not factored into Staff's recommendations herein because they were not known and measurable at the time. However, contractor bids indicated that these repairs could

cost as much as \$89,600, which is more than Hardeman can currently afford to pay out of its cash reserves. Any failure of the tank or another major piece of equipment would adversely affect Hardeman's financial position and threaten its ability to provide adequate water service.

On March 24, 2003, Hardeman filed its rate application to the Commission for consideration. Staff is hereby adopting the contents of Hardeman's application as its recommendation in this report as if fully set out herein. Jason Green is responsible for all revenue adjustments and the calculation of the proposed rates. Jack Kaninberg is responsible for the determination of the revenue requirement. Based on the information included in Hardeman's application, Staff is of the opinion that the rates as shown in Attachment A of this report are reasonable and should be approved by this Commission.

Signatures

Prepared by: Jack Kaninberg
Financial Analyst, Water and Sewer
Revenue Requirements Branch
Division of Financial Analysis

Prepared by: Jason Green
Rate Analyst, Communications, Water,
and Sewer Rate Design Branch
Division of Financial Analysis

ATTACHMENT A
STAFF REPORT CASE NO. 2003-00107
STAFF S RECOMMENDED RATES

Monthly Water Rates

First	2,000 gallons	\$13.10 minimum bill
Next	3,000 gallons	\$ 2.75 per 1,000 gallons
Next	15,000 gallons	\$ 2.12 per 1,000 gallons
Over	20,000 gallons	\$ 1.80 per 1,000 gallons