

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF SOUTH 641 SEWER)
DISTRICT FOR AN ADJUSTMENT)
OF RATES PURSUANT TO THE) CASE NO. 2007-00443
THE ALTERNATIVE RATE FILING)
PROCEDURE FOR SMALL UTILITIES)

O R D E R

On October 22, 2007, South 641 Sewer District ("South 641 Sewer") filed its application for Commission approval of its proposed sewer rates. Commission Staff, having performed a limited financial review of South 641 Sewer's operations, has prepared the attached report containing its findings and recommendations regarding the proposed rates. All parties should review the report carefully and submit any written comments on Staff's findings and recommendations or requests for a hearing or an informal conference within 10 days of the date of this Order.

IT IS THEREFORE ORDERED that all parties shall have 10 days from the date of this Order to submit written comments regarding the attached Staff Report or to request a hearing or an informal conference in this matter. If no request for a hearing or an informal conference is received by that date, this case shall stand submitted to the Commission for decision.

Done at Frankfort, Kentucky, this 28th day of November, 2007.

By the Commission

ATTEST:


Executive Director

STAFF REPORT
SOUTH 641 SEWER DISTRICT
CASE NO. 2007-00443

Pursuant to a request by South 641 Sewer District ("South 641 Sewer") for assistance with the preparation of a rate application, Commission Staff ("Staff") performed a limited review of South 641 Sewer's test year operations for the calendar year ended December 31, 2006. 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 South 641 Sewer 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, as shown in Attachment A. The rates proposed by South 641 Sewer were based on the pro forma income statement as shown in the application. The application also includes the calculation of South 641 Sewer's revenue requirement using a 1.2 Debt Service Coverage, which is frequently used by the Commission to determine revenue requirements for small sewer utilities. To generate the revenue requirement of \$55,585, South 641 Sewer is proposing to increase its annual revenues from sewer rates by \$25,227, an increase of 83.1 percent over normalized sewer revenues of \$30,358.

On October 22, 2007, South 641 Sewer filed its rate application with the Commission. South 641 Sewer's current rate is a flat monthly fee of \$10.95. South 641 Sewer proposes to increase its current rate for sewer-only customers by 79.8 percent to \$19.69, and to charge South 641's joint water/sewer customers a customer charge of \$8.99 and a usage-based charge of \$2.14 per 1,000 gallons. Based on its review, Staff finds that South 641's statement of adjusted test period operations is reasonable and reflective of normal operations and should be used to determine South 641's revenue requirement. Staff further finds that the method that South 641 used to determine its revenue requirement is correct and reasonable. Accordingly, Staff recommends approval of South 641's requested rates.

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 recommendations herein, Staff is of the opinion that the rates as shown in Attachment B 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
Water and Sewer Rate Design Branch
Division of Financial Analysis

ATTACHMENT A
STAFF REPORT CASE NO. 2007-00443

South 641 Attachment A*	2006 Water	2006 Sewer	Comb.	Adjstmnts	Ref	Adjusted Combined	60% Water Exp. Alloc.	40% Sewer
Water Revenue	\$109,774		\$109,774	(\$3,172)		\$106,602	\$106,602	
Sewer Rev.		\$29,304	\$29,304	\$1,054		\$30,358		\$30,358
Total Revenue	\$109,774	\$29,304	\$139,078	(\$2,118)	A	\$136,960		
Empl. Salaries	\$24,227	\$19,822	\$44,049	(\$5,175)	B	\$38,874	\$23,324	\$15,550
Empl. Benefits	\$201	\$164	\$365	\$67	C	\$432	\$259	\$173
Purch. Water	\$34,368	0	\$34,368	0		\$34,368	\$34,368	0
Purch. Power	\$3,008	\$2,461	\$5,469	0	D	\$5,469	\$2,453	\$3,016
Mats/Supplies	\$1,122	\$918	\$2,040	0		\$2,040	\$1,224	\$816
Repairs/Maint.	\$5,929	\$4,851	\$10,780	\$3,600 \$480	E	\$14,860	\$8,800	\$6,060
Office Supplies	\$2,863	\$2,343	\$5,206	0		\$5,206	\$3,124	\$2,082
Contract Serv.	\$3,337	\$2,730	\$6,067	(\$764)	F	\$5,303	\$3,182	\$2,121
Transport. Exp.	\$2,492	\$2,039	\$4,531	0		\$4,531	\$2,719	\$1,812
Insurance	\$1,834	\$1,501	\$3,335	0		\$3,335	\$2,001	\$1,334
Misc. Exp	\$10,312 (5,929) (2,863) \$1,520	\$1,243	\$2,763	0	G	\$2,763	\$1,658	\$1,105
<u>Operating Exp.</u>	<u>\$80,901</u>	<u>\$38,072</u>	<u>\$118,973</u>	<u>(\$1,792)</u>		<u>\$117,181</u>	<u>\$83,112</u>	<u>\$34,069</u>
Depreciation Exp.	\$32,283	\$5,599	\$37,882	Water \$533 \$3,800 Sewer \$2,757	H	\$44,972	\$36,616	\$8,356
Taxes OTI	\$1,844	\$1,546	\$3,390	(\$416)	I	\$2,974	\$1,784	\$1,190
Total Op. Exp.	\$115,028	\$45,217	\$160,245	\$4,882		\$165,127	\$121,512	\$43,615
Net Op. Income	(\$5,254)	(\$15,913)	(\$21,167)	(\$7,000)		(\$28,167)	(\$14,900)	(\$13,257)
Interest Income	\$1,075	\$583	\$1,658	(\$1,658)	J	0	0	0
Nonutil. Income	\$1,317	\$350	\$1,667	(\$1,667)	K	0	0	0
Interest Exp.	(\$9,425)	(\$5,075)	(\$14,500)	0		(\$14,500)	(\$9,425)	(\$5,075)
Net Income	(\$12,287)	(\$20,055)	(\$32,342)	(\$10,325)		(\$42,667)	(\$24,335)	(\$18,332)

Revenue Increase	Combined	Water	Sewer
Operating Expenses	\$165,127	\$121,512	\$43,615
Debt Service Coverage	34,200	\$22,230	\$11,970
Rev. Requirement	\$199,327	\$143,742	\$55,585
Less Normalized Revenues	(136,960)	(106,602)	(30,358)
Justified Increase	\$62,367	\$37,140	\$25,227
Requested Increase	\$56,228	\$31,001	\$25,227
Percentage Increase	41.1%	29.1%	83.1%

Debt Service	2007	2008	2009	Total	3-yr. avg.	X 1.2 DSC
Water Principal	\$8,450	\$9,100	\$9,750	\$27,300	\$9,100	
Water Interest 06	\$9,425				\$9,425	
Total Water DS	\$17,875				\$18,525	\$22,230
Sewer Principal	\$4,550	\$4,900	\$5,250	\$14,700	\$4,900	
Sewer Interest 06	\$5,075				\$5,075	
Total Sewer DS	\$9,625				\$9,975	\$11,970

Reference Notes:

**Please note that joint expenses have traditionally been allocated on a basis of 55% to water and 45% to sewer. In this case, joint expenses have been allocated 60% to water and 40% to sewer to approximate the current ratio of water to sewer customers.*

A. Normalized Water and Sewer Revenues as determined by Commission Staff's billing analysis.

B. Normalized Salaries Expense based on salaries in effect during 2007 for three employees, as follows:

Employee	2006 Salary	Adjustment	Proforma	Notes
Office Manager	\$16,480	(\$16,480)	0	No longer there.
Operator	\$22,294	\$3,380	\$25,674	\$65/ wk. increase
Office Worker	\$5,275	0	\$6,000	\$10 x 50 hrs x 12 mo.
General Manager	0	\$7,200	\$7,200	\$12 x 50 hrs. x 12 mo.
Total	\$44,049	(\$5,175)	\$38,874	

C. Employee Benefits Expense pro forma based on Delta Dental insurance for two employees of \$36 per month, or \$432 per year.

D. Purchased Power Expense has been traditionally allocated by the District between water and sewer operations. Upon closer examination, it appears that \$1,068 of the 2006 purchased power cost could be directly assigned to water operations and \$2,092 could be directly assigned to sewer operations. The remaining \$2,309 of joint costs were allocated 60% to water and 40% to sewer, resulting in additional allocated amounts of \$1,385 for water and \$923 for sewer, and total purchased power amounts of \$2,453 for water and \$3,016 for sewer.

E. Repairs and Maintenance Expense totaled \$10,780 combined in 2006, and was allocated 55% to water and 45% to sewer according to the 2006 PSC Annual Reports. Upon closer examination, amounts totaling \$4,738 for water and \$5,751 for sewer could be directly assigned. An additional \$292 of joint costs were allocated 60% to water and 40% to sewer, resulting in test period repair expenses of \$4,913 for water and \$5,868 for sewer.

In addition, an adjustment was made to recognize new water testing expenses of \$3,600 which South 641 will incur on a pro forma basis. Finally, another adjustment

was made to recognize additional fuel expenses of \$480 which South 641 will incur from a testing contractor, and those expenses were allocated 60% to water and 40% to sewer, resulting in total pro forma Repairs and Maintenance Expense of \$8,800 for water and \$6,060 for sewer.

F. Contract Services Expense was adjusted to remove \$764 of nonrecurring contract service payments.

G. Water Miscellaneous Expense of \$10,312 per the 2006 PSC Annual Report was adjusted to reclassify water Repairs Expenses and Office Supplies into those accounts, reducing Water Miscellaneous Expense to \$1,520 before allocations.

H. Depreciation Expense was adjusted to include the Depreciation Expense on certain projects needed to provide adequate service, as follows:

Project	Estimated cost-(Materials only)	Useful Life (yrs.)	Annual amount (Mats. Only)
Water			
Telemetry System Replacement	\$20,000	10	\$2,000
4 New Shut-off valves this year	\$18,000	10	\$1,800
Total Water Depreciation Adj.	\$38,000		\$3,800
Sewer			
New Flow Meter	\$8,000	10	\$800
Chlorination system	\$11,000	10	\$1,100
Waste Water Pump	\$6,000	7	\$857
Total Sewer Depreciation Adj.	\$25,000		\$2,757

In addition, water depreciation expense was adjusted to include additional depreciation expense for meters that South 641 had been depreciating over 5 years. The Commission's Engineering Branch normally uses a 10-year life for water meter replacements, resulting in an adjustment of \$533, as follows:

Date	Amount	Over 10 yrs.	2006 @ 5 yrs.
8/15/98	\$449.00	\$44.90	0
8/1/98	\$3,801.00	\$380.10	0
7/1/99	\$8,398.00	\$839.80	0
7/1/00	\$4,885.50	\$488.55	0
7/1/01	\$2,642.00	\$264.20	\$264.20
7/1/02	\$3,171.50	\$317.15	\$634.30
7/1/03	\$2,704.50	\$270.45	\$540.90
7/1/04	\$3,494.32	\$349.43	\$698.86
7/1/05	\$2,827.50	\$282.75	\$565.50
7/1/06	\$6,610.00	\$661.00	\$661.00
		\$3,898.33	\$3,364.76
		Proper Amt.	Booked Amt.
		Increase	\$533.57

I. Taxes Other Than Income Expense was adjusted to reflect pro forma FICA taxes of \$2,974 based on pro forma Salaries Expense of \$38,874 x 7.65%.

J. Interest Income was removed because South 641 has drawn down its reserves - most of which are restricted - to pay expenses.

K. Nonutility Income was adjusted to remove \$1,667 of nonrecurring revenue.

ATTACHMENT B
STAFF REPORT CASE NO. 2007-00443
STAFF'S RECOMMENDED RATE

Monthly Sewer Rate

Customer Charge
Per 1,000 gallons

\$8.99 minimum bill
\$2.14 per 1,000 gallons

Monthly Sewer Rate for Sewer Customers Only

Flat Rate Minimum Bill

\$19.69 minimum bill