

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ALTERNATIVE RATE ADJUSTMENT FILING OF) CASE NO. 2013-00170
WOOD CREEK WATER DISTRICT)

ORDER

Wood Creek Water District ("Wood Creek District") has applied to adjust its rates for sewer service. By this Order, the Commission approves rates that will produce annual revenues of \$632,491, an increase of \$253,429 or 66.85 percent, over pro forma present rate revenues. Our action will increase the monthly sewer bill of a residential customer who uses 5,000 gallons of water monthly from \$25.40 to \$42.37, or 66.8 percent.

On June 3, 2013, Wood Creek District applied for a rate adjustment pursuant to 807 KAR 5:076.¹ On July 22, 2013, after reviewing the application and Wood Creek District's records, Commission Staff issued a report containing its findings regarding the proposed rate adjustment. Commission Staff found that Wood Creek District's proposed rates would generate additional revenues of \$121,251 over pro forma test-year revenues.² It further found that, using the operating ratio to determine Wood Creek District's revenue requirements, Wood Creek District's financial condition would support

¹ Wood Creek District tendered its application for rate adjustment to the Commission on April 14, 2013. As Wood Creek District had failed to publish notice of the proposed adjustment in accordance with 807 KAR 5:076, Section 5, its application was not accepted for filing. On June 3, 2013, after Wood Creek District submitted evidence of publication of proper notice, the Commission accepted the application for filing.

² Staff Report at 2-3. Commission Staff found that Wood Creek District's proposed rates will produce revenues from sewer service of \$500,313 and that Wood Creek District's existing rates produce revenues of \$379,062. $\$500,313 - \$379,062 = \$121,251$.

a revenue requirement from its sewer operations of \$878,937 and, therefore, a revenue increase of \$499,875.³ Commission Staff also recommended that the Commission direct Wood Creek District to revise its method for calculating and recording depreciation expense for accounting and ratemaking purposes and to revise its methods of allocating shared transactions between its water and sewer divisions.⁴

In response to this report, Wood Creek District advised the Commission that it did not object to Commission Staff's findings and further requested rates that would generate revenue from sewer sales in the amount of \$632,491. Wood Creek stated that "the revised proposed rate adjustment will significantly relieve the existing unacceptable financial condition of the sewer division operation while considering the impact of the increased cost on the sewer customers."⁵

On August 7, 2013, Wood Creek District published in a newspaper of general circulation in its territory notice of its revised proposed rates.⁶ On September 1, 2013, having received no comments on Wood Creek District's request nor requests for intervention in this proceeding, the Commission closed the record and submitted the matter for decision.

Having reviewed the evidence of record and being otherwise sufficiently advised, the Commission finds that:

³ *Id.* at 10.

⁴ *Id.* at 3.

⁵ Wood Creek Water District's Response to the Order of July 26, 2013 at 1 (filed Aug. 2, 2013).

⁶ Letter from Dewayne Lewis, Office Manager, Wood Creek Water District, to Jeff Derouen, Executive Director, Public Service Commission (Aug. 7, 2013).

1. Wood Creek District, a water district organized pursuant to KRS Chapter 74, owns and operates sewage collection facilities that serve approximately 1,135 customers in Laurel County, Kentucky.⁷

2. The calendar year ending December 31, 2012, should be used as the test year to determine the reasonableness of Wood Creek District's existing and proposed rates.⁸

3. Based upon pro forma test-year sewer operations, Wood Creek District's total pro forma revenue is \$385,141.⁹

4. Based upon pro forma test-year sewer operations, Wood Creek District's total pro forma operating expenses, after adjusting for known and measurable changes, is \$778,814.¹⁰

5. The statement of Wood Creek District's test-period sewer operations, as adjusted for known and measurable changes, is set forth in Appendix A of this Order.

6. Wood District presently uses service lives for five classes of assets that are at variance¹¹ with those found in a survey issued by the Commission on Rural Water.¹²

⁷ *Annual Report of Wood Creek Water District to the Public Service Commission of Kentucky for the Calendar Year Ending December 31, 2012 (Sewer Division)* at 1 and 8. See also Kentucky Infrastructure Authority, *Kentucky Wastewater Management Plan 257* (Apr. 2013).

⁸ 807 KAR 5:076, Section 8.

⁹ Staff Report at 4. \$379,062 (Operating Revenues) + \$6,068 (Miscellaneous Sewage Revenues) + \$11 (Interest and Dividend Income) = \$385,141.

¹⁰ *Id.*

¹¹ *Id.* Attachment C.

¹² Commission on Rural Water, *Guide for the Support of Rural Water-Wastewater Systems* (Chicago, Ill. 1974) 246-247.

7. The Commission has previously used the same survey to establish the service lives of utility assets.¹³

8. The record contains no evidence that the service lives that Wood Creek District uses are based upon a depreciation study or its own historic plant records.

9. Wood Creek District's assignment of service lives for these five classes of assets is not reasonable and should be revised for ratemaking and accounting purposes.¹⁴

10. Appendix B to this Order sets forth the classes of assets whose service lives should be adjusted, the previously assigned service life of each class, the service life range that the Commission on Rural Water survey suggests for each class, and the assigned service life that should be used for ratemaking and accounting purposes for all future reporting periods.

11. As of December 31, 2012, Wood Creek District had no outstanding long-term debt.

¹³ See, e.g., Case No. 2004-00336, *Joint Application of B & H, Inc. and Richmond Utilities, LLC for Approval of the Transfer of Wastewater Treatment Plant to Richmond Utilities, LLC* (Ky. PSC Dec. 22, 2004).

¹⁴ These reassignments require a reduction of \$85,841 in Wood Creek District's test-period depreciation expense. Staff Report at 8.

12. Since Wood Creek District has no outstanding long-term debt, the use of an operating ratio¹⁵ is the most appropriate methodology to determine Wood Creek District's revenue requirement.¹⁶

13. An operating ratio of 88 percent will permit Wood Creek District to meet its reasonable operating expenses and provide for a reasonable operating margin and should be used to determine Wood Creek District's total revenue requirement.

14. Applying an operating ratio of 88 percent to Wood Creek District's pro forma operating expenses of \$778,814, Wood Creek District has a total revenue requirement of \$885,016.¹⁷

15. Based upon pro forma test-year sales, Wood Creek District's proposed rates will produce annual revenues from sewer operations of \$500,313.

16. Based upon pro forma test-year sales, Wood Creek District's revised proposed rates will produce annual revenues from sewer operations of \$632,491, an increase of \$253,429 over test-period pro forma revenues from sewer operations.

17. Wood Creek District's revised proposed rates, which are set forth in Appendix C to this Order, will produce a level of revenue that is sufficient to meet its sewer operations' reasonable operating expenses and will produce cash working capital

¹⁵ Operating Ratio is defined as the ratio of expenses, including depreciation and taxes, to gross revenues. It is illustrated by the following equation:

$$\text{Operating Ratio} = \frac{\text{Operating Expenses} + \text{Depreciation} + \text{Taxes}}{\text{Gross Revenues}}$$

¹⁶ See, e.g., Case No. 8468, *An Adjustment of the Rates of Plantation Hill Sewage Treatment Plant, Inc.* (Ky. PSC June 25, 1982); 1 A.J.G Priest, *Principles of Public Utility Regulation* (Michie 1969) 220-224.

¹⁷ \$778,814 (Pro Forma Operating Expenses) ÷ 0.88 = \$885,016 (Total Revenue Requirement).

of \$159,914.¹⁸ Implementation of these rates is not likely to cause the sewer service that Wood Creek District renders to the public to suffer.

18. Where a utility has requested rates that are less than a regulatory commission determines “would furnish a fair return then, in the absence of some factor which would in the public interest require that larger rates be charged, the rates requested by the utility ought to be allowed.”¹⁹

19. The rates set forth in Appendix C should be charged by Wood Creek District for service rendered on and after the date of this Order.

20. In its financial and statistical reports for its water and sewer operations for the year ending December 31, 2012, Wood Creek District failed to allocate shared transactions between its water and sewer divisions, but instead assigned the total expense or revenue to its water division. The failure to properly allocate such transactions results in the inaccurate reporting of Wood Creek District’s financial condition.

21. Wood Creek District should revise its accounting procedures and internal controls to reasonably and fairly assign and allocate shared transactions between its water and sewer divisions.

¹⁸ \$632,491 (Revised Requested Revenue Requirement) + \$6,068 (Other Operating Revenue) + \$11 = \$638,570 (Net Available for Operations). \$638,570 - \$478,656 (Pro Forma Operation and Maintenance Expense) = \$159,914.

¹⁹ *Utilities Operating Co. v King*, 143 So.2d 854, 45 PUR3d 439, 443 (Fla. 1962) (“[I]n the absence of some showing that the service to the public will suffer by allowing . . . [a] utility to charge rates which will not produce a fair return, the utility and not the Commission has the right of decision as to the rates it will charge so long as they do not exceed those which would produce a fair return as determined by the Commission.”). See also Case No. 2006-00410, *The Application of Hardin County Water District No. 1 for a General Rate Adjustment Effective On and After December 2, 2006* (Ky. PSC Aug. 2, 2007); Case No. 98-398, *Adjustment of Rates of the Kentucky Turnpike Water District and the Imposition of an Impact Fee* (Ky. PSC June 30, 1999).

IT IS THEREFORE ORDERED that:

1. Wood Creek District shall, for accounting and ratemaking purposes, use the "PSC Approved Service Life" set forth in Appendix B to this Order for the listed classes of assets when calculating and reporting depreciation for all reporting periods after the date of this Order, but shall make no retroactive adjustment to its books to account for the cumulative effect of this change in accounting estimate.

2. Wood Creek District's originally proposed rates are denied.

3. Wood Creek District shall charge the rates set forth in Appendix C to this Order for sewer service rendered on and after the date of this Order.

4. Within 20 days of the date of this Order and using the Commission's Electronic Tariff Filing System, Wood Creek District shall file with the Commission revised tariff sheets that contain the rates set forth in Appendix C.

5. Within 90 days of the date of this Order, Wood Creek District shall revise its accounting procedures and internal controls to include methods and practices that reasonably and fairly allocate revenues and expenses between its water and sewer divisions and shall file with the Commission a copy of these revised procedures and controls and evidence of its Board of Commissioners' formal adoption of such procedures.

6. Any documents filed pursuant to ordering paragraph 5 shall reference this case number and shall be retained in the utility's general correspondence file.

7. The Executive Director is delegated authority to grant reasonable extensions of time for the filing of any documents required by this Order upon Wood Creek District's showing of good cause for such extension.

By the Commission

ENTERED
NOV 12 2013
KENTUCKY PUBLIC
SERVICE COMMISSION

ATTEST:

David D. Gruenewald
Executive Director

Case No. 2013-00170

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2013-00170 DATED NOV 12 2013

Adjusted Operating Statement For
Wood Creek Water District (Sewer Operations)

Operating Revenue	
Operating Revenues – Measured	\$379,062
Miscellaneous Sewage Revenues	<u>6,068</u>
Total Operating Revenue	<u>385,130</u>
Operating Expenses	
Operation and Maintenance Expenses:	
Fuel and Power	24,026
Chemicals	49,827
Miscellaneous Supplies and Expenses -	
Collection	2,242
Maintenance – Collection System	11,636
Maintenance – Treatment and Disposal	47,955
Maintenance – Other Plant Facilities	25,556
Administrative and General Salaries	38,610
Office Supplies and Other Expenses	14,625
Outside Services Employed	232,337
Insurance	14,118
Transportation	<u>17,724</u>
Total Operation and Maintenance Expenses	478,656
Depreciation	299,153
Amortization Expense	<u>1,005</u>
Total Operating Expenses	<u>778,814</u>
Net Operating Income	(393,684)
Interest and Dividend Income	<u>11</u>
Net Income	<u>\$ (393,673)</u>

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2013-00170 DATED NOV 12 2013

Proposed Modifications to the Service Lives of
Certain Assets of Wood Creek Water District (Sewer Operations)

Asset Class	Wood Creek District Acct. No.	Commission On Rural Water Range	Previous Assigned Service Life	PSC Approved Service Life
Pumps	544	20 - 50 years	7 years	35 years
56,264 Service Lines	548	10 years	40 years	10 years
Services	591	10 years	20 years	10 years
Electric Pumping Equipment	577	20 – 50 years	20 years	35 years
Electric Pumping Equipment	592	7 years	20 years	7 years

APPENDIX C

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2013-00170 DATED NOV 12 2013

The following rates and charges are prescribed for the customers in the area served by Wood Creek Water District for sewer service rendered on and after the date of this Order. 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 effective date of this Order.

Monthly Water Rates

5/8-Inch x 3/4-Inch Meter

First	2,000 gallons	\$20.69	Minimum bill
Next	1,500 gallons	7.50	per 1,000 gallons
Next	1,500 gallons	6.95	per 1,000 gallons
Next	2,500 gallons	6.23	per 1,000 gallons
Over	7,500 gallons	5.43	per 1,000 gallons

1-Inch Meter

First	5,000 gallons	\$42.37	per 1,000 gallons
Next	2,500 gallons	6.23	per 1,000 gallons
Over	7,500 gallons	5.43	per 1,000 gallons

2-Inch Meter

First	20,000 gallons	\$125.82	per 1,000 gallons
Over	20,000 gallons	5.43	per 1,000 gallons

3-Inch Meter

First	30,000 gallons	\$180.12	per 1,000 gallons
Over	30,000 gallons	5.43	per 1,000 gallons

6-Inch Meter

First	100,000 gallons	\$560.22	per 1,000 gallons
Over	100,000 gallons	5.43	per 1,000 gallons

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