

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION OF KENTUCKY

In the Matter of:

Electronic Application of Water Service)
Corporation of Kentucky for a General) Case No. 2018-00208
Adjustment in Existing Rates)

**PETITION FOR REHEARING OF
WATER SERVICE CORPORATION OF KENTUCKY**

Pursuant to KRS 278.400, Water Service Corporation of Kentucky (“WSCK”), by counsel, petitions the Public Service Commission of Kentucky (“Commission”) for rehearing of its February 11, 2019, Order. WSCK respectfully requests that the Commission modify its order on the following issues: (1) adjust CIAC amortization expense so that the CIAC amortization rates match the depreciation rates authorized by the Commission; (2) approve WSCK’s requested tariff changes; (3) authorize WSCK to reconcile the actual TCJA refund to the ordered TCJA refund if the difference exceeds a 5-percent variance; (4) correct a clerical error to show that the test year ended December 31, 2017; (5) authorize WSCK to recover rate case expense for this Petition; and (6) include CIAC amortization expense as a component of taxable income, which adjust income tax expense, as the Commission has consistently done. In support of this Petition, WSCK states the following:

I. CIAC amortization rates should match the depreciation rates authorized by the Commission.

Contributions-in-Aid of Construction (“CIAC”) are payments made by customers generally to fund plant additions for new or expanded service. The Commission generally does not allow depreciation expense to be included in rates on investor-owned utility plant funded by CIAC, finding that it would result in a double recovery of plant investment from contributors. In order to exclude depreciation expense on utility plant funded by CIAC, regulatory accounting requires the inclusion of CIAC amortization as an offset to depreciation expense. Therefore, by including both the depreciation and CIAC amortization from utility plant funded by CIAC, the depreciation expense is eliminated. When CIAC amortization expense and the corresponding depreciation expense is included for ratemaking purposes, regulatory accounting requires that the CIAC and utility plant in service be amortized or depreciated over the same time period. This ensures that CIAC and the utility plant are synchronized. This is consistent with the Uniform System of Accounts accepted by this Commission.¹

In the current case, the Commission determined that WSCK should adjust its current depreciation rates to be based on the average life range for each asset group found appropriate in the National Association of Regulatory Utility Commissioners Study of Depreciation Practices for Small Water Utilities (“NARUC Study”). By changing the depreciation rates for WSCK’s assets, the amortization period for WSCK’s CIAC should have received a commensurate change. It does not appear that the Commission made that change.

In Appendix B of the Commission’s Order, the Commission does not amend WSCK’s pro forma amount of (\$14,627) for Amortization of CIAC.² This amount, however, was

¹ See National Association of Regulatory Utility Commissioners, “Uniform System of Accounts for Class A/B Accounts” (1996), as modified by the Kentucky Public Service Commission (2002) at 11, 31, 42.

² See also WSCK Application, Schedule B, line 42.

calculated based on the depreciation rates that were rejected by the Commission. Workpaper [f] in the WCK's Application shows that calculation, and it was not changed by the Commission's order.

When the Commission ordered WCK to amend its depreciation rates to be consistent with the NARUC Study, the CIAC amortization rates and corresponding CIAC dollar amount should have been adjusted. The CIAC-Meters account should be amortized with a rate of 2.25% based on the Commission-approved depreciation rate for meters; the CIAC-Other Tangible Plant account should be amortized with a rate of 2.86% based on the Commission approved depreciation rate for other tangible plant; and the CIAC-Water-Tap account should be amortized with a rate of 2.50% based on the Commission approved depreciation rate for service lines.³ The Commission's ordered calculation and the corrected calculation based on the Commission's decision on depreciation are as follows:⁴

Case No. 2018 - 00208
 Amortization Expense
 Test Year Ended 12/31/2017

Account ID	Account Description	12/31/2017 Test Year	Commission Order Amortization Rate	Commission Order CIAC Amortization	Corrected Amortization Rate	Corrected CIAC Amortization
3350	CIAC-METERS	\$ (83,141)	5.80%	\$ (4,822)	2.25%	\$ (1,871)
3430	CIAC-OTHER TANGIBLE PLT W	(104,819)	3.33%	(3,494)	2.86%	(2,995)
3435	CIAC-WATER-TAP	(189,326)	3.33%	(6,311)	2.50%	(4,733)
Total Amortization of CIAC				\$ (14,627)		\$ (9,599)

This is consistent with the Commission's prior practice in WCK rate cases. For example, in 2011, the Commission approved⁵ WCK's adjustment to reflect that CIAC would be amortized consistent with the utility's practice (at the time) of a 2-percent composite

³ The PSC-approved depreciation rates can be found in WCK's Response to PSC Staff's Second Request, Item 24(d).

⁴ Contemporaneous to the filing of this Petition, WCK is filing an Excel workbook containing this calculation and other workpapers related to this Petition. This workbook is marked as Exhibit 1.

⁵ *Water Service Corp. of Kentucky*, Case No. 2010-00476 at 14 (Ky. PSC Nov. 23, 2011).

depreciation rate.⁶ Similarly, in 2014, the Commission increased the CIAC amortization to reflect customer advances.⁷

Ultimately, by matching the CIAC amortization rates with the depreciation rates authorized by the Commission, the CIAC amortization expense should be a credit balance of (\$9,599). WSCK respectfully requests that the Commission make the necessary adjustment to WSCK's revenue requirement and rates to correct amortization expense.

II. The Commission should explicitly approve WSCK's proposed amendments to its tariff.

In its application, WSCK proposed several changes to the provisions of its tariff. The Commission did not address these items in its final order. These items were discussed in WSCK's post-hearing brief, beginning on page 15. The Office of Attorney General did not present any argument in opposition of WSCK's proposed tariff changes in its post-hearing brief.

On Sheet 13, WSCK proposes to add two new provisions that authorize WSCK to recover the costs associated with re-locating or raising WSCK's portion of the service line. These two additional provisions are designed to allow the utility to recoup expenses from the cost-causer, as opposed to socializing costs to the customer base.

WSCK proposes to clarify a provision on Sheet 19 to reflect the intent of the provision. The intent of Rule 14(c) was undoubtedly to provide notice that the Company was authorized to pursue lawful remedies, such as collection actions, in order to recover amounts owed by customers regardless of whether the Company disconnected service. WSCK is inserting the word "not" to reflect the intent of the provision.

On Sheet 34, WSCK is proposing a provision that allows the Company to require an encasement pipe on a customer's service line. An encasement pipe would typically be required

⁶ See Testimony of Brian Shrake, Case No. 2010-00475 at 6 (filed Jan. 24, 2011).

⁷ *Water Service Corp. of Kentucky*, Case No. 2013-00237 at 22 (July 24, 2014).

when a customer's line is under vehicle traffic and causes additional external stress and or pressure on the pipe.⁸ An encasement pipe is designed protect against unnecessary damage and costs to the utility.

WSCK also seeks to add a provision on Sheet 37 in its tariff that authorizes the utility to recover all costs associated with having to repair and replace meters and fixtures when a customer tampers with the meter. This is another provision that is designed to place responsibility for expenses on the cost-causer of those expenses.

WSCK respectfully requests that the Commission explicitly approve these changes to the four sheets in its tariff.

III. The Commission should authorize WSCK to reconcile the amount of the TCJA refund if it exceeds a 5-percent variance.

The Commission determined that WSCK should refund \$54,199 to customers, in order to account for the impact of the Tax Cut and Jobs Act on WSCK.⁹ It calculated, and accordingly ordered, a surcredit of \$0.13 per 1,000 gallons to be refunded to customers for a twelve-month billing period.¹⁰ WSCK is not requesting reconsideration of the total amount to be refunded to customers, but rather, is merely requesting a true-up if certain circumstances are met.

Specifically, WSCK requests the opportunity to reconcile the refund amount of \$54,199 at the end of the refund period (February 11, 2020) if the amount refunded to customers is above or below a 5-percent variance from the \$54,199 amount. If the amount of the refund is less than \$51,489 or if the amount of the refund was greater than \$56,909, WSCK will true-up the amount

⁸ See WSCK Response to Staff's Second Request for Information, Item 22.

⁹ Order at 15.

¹⁰ In footnote 40 of the Order, the Commission erroneously identified the number of gallons during the test-year as 407,717,112. The calculation of \$0.13 does not change using the correct number of 408,717,112 gallons, as identified in the body of the Order.

of the refund in one billing cycle. If one of these circumstances existed, WSCK would provide documentation to the Commission to verify the amount of the true-up and refund.

WSCK believes this is consistent with the Commission's intent. First and foremost, the true-up mechanism is designed to protect both the customers and the utility from under- or over-recovery of revenue. Second, there is support for this in Commission decisions. In the present case, the Commission stated that it would "follow the same methodology in terms of rate design as it did in Case Nos. 2018-00040 and 2018-00041."¹¹ In 2018-00041, the Commission approved Columbia Gas's request to reconcile and true-up the amounts related to the utility's refund of federal income tax liability.¹² WSCK is seeking a similar opportunity. WSCK respectfully requests that the Commission allow a reconciliation of the TCJA refund amount of \$54,199 at the end of the refund period if the actual amount refunded to customers is above or below a 5-percent variance from \$54,199.

IV. The Order should be corrected to reflect the test year ending December 31, 2017.

In enumerated paragraph number 1 of page 15 of the Order, it states that the "12-month period ending June 30, 2017, should be used as the test year to determine the reasonableness of Water Service Corporation of Kentucky's current and proposed rates. Other statements in the Order accurately reflect the proposed rates and relevant data submitted in the case related to a historic-test year ending on December 31, 2017. The Commission should correct this clerical error.

¹¹ *Id.*

¹² *See Columbia Gas Co.*, Case No. 2018-00041 at 6 (Ky. PSC Oct. 25, 2018).

V. The Commission should allow WSCK to recover rate case expense for this Petition for Rehearing.

The Commission has acknowledged that “[i]t is a well-settled principle of utility law that rate case expenses ‘must be included among the costs of operation in the computation of a fair return.’”¹³ Likewise, it has stated that a utility is entitled “to recover all prudent and reasonable rate case costs.”¹⁴

The present circumstances demonstrate that WSCK is incurring prudent and reasonable rate-case expense in this Petition for Rehearing. The vast majority of issues that are raised—CIAC amortization rates to match depreciation rates, CIAC amortization to be included in income tax calculations, omission of tariff amendment approvals, and erroneous statements of the test-year period—appear to be mere oversights on behalf of the Commission. Accordingly, WSCK’s expenses associated with this Petition are prudent and reasonable.

WSCK has incurred \$4,196 in expenses related to this Petition,¹⁵ as evidenced in the legal invoice submitted in Exhibit 2. WSCK has not included costs incurred for review of the final order or issues related to customer notice of Ambleside subdivision because these costs are not directly associated with this Petition. Amortized over the Commission-ordered 3-year period, this would increase operating expense by \$1,398.67.

¹³ *Kentucky-American Water Co.*, Case No. 2010-00036 (Ky. PSC. Dec. 14, 2010)(quoting *Ohio Gas Co. v. Pub. Utils. Comm’n of Ohio*, 294 U.S. 63, 73 (1935)).

¹⁴ *Kentucky-American Water Co.*, Case No. 97-034 at 23 (Ky. PSC. Sept. 30, 1997).

¹⁵ WSCK believes the Commission can grant the Petition for Rehearing and grant the relief requested without additional evidence or argument. To the extent the Commission establishes additional proceedings to determine the reasonableness of WSCK’s position contained herein, WSCK respectfully requests the opportunity to amend this amount.

VI. Amortization of CIAC and the rate case expense associated with this Petition should be included within the taxation calculation.

On page 17 of the Order, the Commission calculated the pro-forma income-tax expense. The Commission, however, omitted CIAC amortization expense in the calculation of income-tax expense. CIAC amortization expense has consistently been included in the Commission's calculation of WSCK's income-tax expense in past rate cases.¹⁶ As discussed in the section above, the appropriate CIAC amortization expense that should have been included in the calculation of income-tax expense was \$9,599. Similarly, the addition of rate case expense associated with this Petition for Rehearing of \$1,398.67 should be included within the General Expense category. The addition of the appropriate CIAC amortization expense and rate case expense changes the pro-forma income-tax expense from (\$27,457) to (\$25,412), as shown below:

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¹⁶ See *Water Service Corp. of Kentucky*, Case No. 2013-00237 at Table II, page 26; *Water Service Corp. of Kentucky*, Case No. 2010-00476 at Table I, page 16; *Water Service Corp. of Kentucky*, Case No. 2008-00563 at Table III, page 19 (Ky. PSC Nov. 9, 2009). For ease of reference, these tables are attached collectively as Exhibit 3.

WATER SERVICE CORPORATION OF KENTUCKY
Case No. 2018 - 00208
Calculation of State and Federal Income Tax
Test Year Ended 12/31/2017

Description	Commission Order	Petition for Rehearing
Operating Revenue	\$ 2,479,383	\$ 2,479,383
Add:		
Income from Management Services	177,741	177,741
Less:		
Maintenance Expense	(1,213,464)	(1,213,464)
General Expense	(754,824)	(756,223)
Depreciation	(443,320)	(443,320)
Amortization of CIAC	-	9,599
Taxes Other Than Income	(183,615)	(183,615)
Total Operating Expenses (Net Income Tax Exp.)	(2,595,223)	(2,587,023)
Interest Expense	(171,951)	(171,951)
Taxable Income	\$ (110,050)	\$ (101,850)
State Income Tax Rate	5%	5%
Pro Forma State Income Tax Rate	\$ (5,502)	\$ (5,093)
Federal Taxable Income	(104,548)	(96,758)
Federal Tax Rate	21%	21%
Total Federal Taxes	\$ (21,955)	\$ (20,319)
Total Proforma Income Tax Expense	\$ (27,457)	\$ (25,412)

As calculated above, this change results in an adjustment of \$2,405 in income-tax expense, and WSCK respectfully requests that the Commission make appropriate adjustments to WSCK's revenue requirement and rates to correct income tax expense.

VII. Proposed Revenue Requirement and Rates

Based on the information above, WSCK respectfully requests the Commission grant its Petition for Rehearing and authorize a revenue requirement of \$548,010. This calculation is shown in the table below.

WATER SERVICE CORPORATION OF KENTUCKY
Case No. 2018 - 00208
Revenue Requirement
Test Year Ended 12/31/2017

Line No.	Item	Commission Order	Petition for Rehearing
1.	Total Operating Expenses	\$ 2,375,398	\$ 2,383,871
2.	Less: Federal & State Income Taxes	27,457	25,412
3.			
4.	Operating Expenses Net of Income Taxes	\$ 2,402,855	\$ 2,409,282
5.	Divide by: Operating Ratio	88%	88%
6.			
7.	Revenue to Cover Operating Ratio	\$ 2,730,517	\$ 2,737,821
8.	Less: Operating Expenses Net of Income Taxes	\$ (2,402,855)	\$ (2,409,282)
9.			
10.	Net Operating Income After Income Taxes	\$ 327,662	\$ 328,538
11.	Less: Pro Forma Net Income	66,941	75,414
12.			
13.	Net Operating Income Adjustment	\$ 394,603	\$ 403,952
14.	Multiplied by Gross-up Factor	1.356621985	1.356621985
15.			
16.	Revenue Requirement	\$ 535,327	\$ 548,010
17.			
18.	Percentage Increase/Decrease	22.15%	22.68%

For simplicity, WSCK proposes the difference in revenue of \$12,683 between this amount and the amount previously authorized by Commission order on February 11, 2019, be applied to the volumetric rate only. This would increase the volumetric rates by three cents to the following:

Tier 1 - First 100,000 gallons	\$5.08
Tier 2 - Over 100,000 gallons	\$3.48

WHEREFORE, on the basis of the foregoing, WSCK respectfully petitions the Commission to issue an Order granting rehearing and awarding the relief requested herein.

Respectfully submitted,



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ATTORNEYS FOR WATER SERVICE CORPORATION
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EXHIBIT 1

EXCEL WORKPAPER



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STATEMENT OF SERVICES

Employer I.D. No. 61-0576615

Statement Date: 02/25/2019
Account No: 64592.0008 M
Statement No: 117858

WSCK Rate Case 2018 - 2018064.2906

2018064.2906

			Hours
02/11/2019	MTO	Review final order from the PSC; draft summary of order to send to client;	1.00
	MTO	Review additional PSC decisions on potential Petition for Rehearing.	0.50
02/13/2019	MTO	Communicate with attorney JWG to discuss strategy for petition for rehearing	0.20
	JWG	Communicate (in firm) with T.Osterloh regarding order and issues for rehearing.	0.20
02/14/2019	MTO	Draft/revise - draft communications with client regarding notice requirements for Ambleside subdivision surcharge	0.80
02/15/2019	MTO	Communicate (with client) - phone call with Steve Lubertozzi and Rob Guttormsen regarding petition for appeal topics	0.80
	MTO	Draft/revise - begin drafting brief for Petition for Rehearing.	3.80
02/16/2019	MTO	Draft/revise - continue drafting and researching issues on petition for rehearing on CIAC.	1.60
02/18/2019	MTO	Communicate (with client) with Steve Lubertozzi regarding Petition for Rehearing	0.20
	MTO	Communicate (with client) - phone call with Rob Guttormsen regarding Petition for Rehearing	0.20
02/19/2019	MTO	Review affidavit to be filed in support of PSC Order verifying that notice was issued to Ambleside customers; communicate with Guttormsen regarding Ambleside notice and revised tariffs.	0.50
02/20/2019	MTO	Draft/revise - continue drafting petition for rehearing on CIAC, TCJA, and tariff provisions; communicate with R. Guttormsen regarding same.	4.50

Note: Copy of E-mail only statement.

Exhibit 2

Utilities, Inc.

02/25/2019

Account No. 64592-0008M

Invoice No. 117858

WSCK Rate Case 2018 - 2018064.2906
2018064.2906

			Hours		
02/21/2019	MTO	Draft/revise - continued work on Petition for Rehearing on issues related to test year and rate case expense; communicate with R. Gutormsen regarding same.	1.30		
02/22/2019	MTO	Draft/revise - continued drafting of Petition for Rehearing on rates; revisions of Petition; communication with client regarding same.	2.70		
02/25/2019	JWG	Review and revise Petition for Rehearing For Current Services Rendered	0.80		
			19.10	4,759.50	

Recapitulation

<u>Timekeeper</u>	<u>Title</u>	<u>Hours</u>	<u>Hourly Rate</u>	<u>Total</u>
M. Todd Osterloh	Member	18.10	\$245.00	\$4,434.50
James W. Gardner	Of Counsel	1.00	325.00	325.00
Total Current Work				4,759.50
Previous Balance				\$20,810.50
Balance Due				\$25,570.00

Past Due Amounts

<u>Stmt Date</u>	<u>Stmt #</u>	<u>Billed</u>	<u>Due</u>
01/11/2019	117131	20,810.50	20,810.50
			20,810.50

PAYMENT DUE UPON RECEIPT
 To ensure proper credit to your account
 Please write Account 64592.0008 on your check
 Thank you

Note: Copy of E-mail only statement.

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF WATER SERVICE)	CASE NO.
CORPORATION OF KENTUCKY FOR AN)	2013-00237
ADJUSTMENT OF RATES)	

ORDER

On September 27, 2013,¹ Water Service Corporation of Kentucky (“WSKY”), a Kentucky Corporation, filed its application requesting rates that will produce additional revenues from water sales of \$228,789, or approximately 10.9 percent. WSKY later revised its requested increase in annual revenues from water sales to \$233,411, or approximately 11.1 percent. By this Order, the Commission establishes rates that will produce additional revenues from water sales of \$84,719, or an increase of 3.95 percent. For a customer who has a 5/8- x 3/4-inch meter and uses 5,000 gallons of water monthly, these rates will result in an increase of \$0.96 in the monthly bill for a customer residing in Bell County or \$1.56 for a customer residing in Hickman County.

BACKGROUND

WSKY provides water service for compensation to 607 customers in Hickman County, Kentucky, and 5,900 customers in Bell County, Kentucky.² WSKY is a wholly owned subsidiary of Utilities, Inc. (“UI”), an Illinois corporation that indirectly owns over 70 water and wastewater systems in 15 states throughout the United States. Water

¹ Pursuant to 807 KAR 5:001, Section 8(2), WSKY gave notice on June 20, 2013, of its intent to file an application for a rate adjustment using the electronic filing procedures set forth in that regulation.

² Refer to WSKY’s Response to the Initial Information Request submitted by the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention (“AG”), Item 1.

expenses determined reasonable herein, the Commission arrives at its pro forma income tax expense of \$114,281 as shown in the Table II below.

Table II: Income Tax

	State	Federal
Operating Revenues	\$ 2,225,468	\$ 2,225,468
Operating Expenses:		
Maintenance and General Expense	1,574,640	1,574,640
Depreciation & Amortization	205,141	205,141
Amortization CIAC & AIAC	(9,850)	(9,850)
Taxes Other Than Income	143,579	143,579
Income from Management Services	(153,285)	(153,285)
State Income Tax		18,063
Operating Expenses	<u>1,760,225</u>	<u>1,778,288</u>
Taxable Income before Interest Expense	465,243	447,180
Less: Interest Expense	<u>(164,188)</u>	<u>(164,188)</u>
Taxable Income	301,056	282,993
Multiplied by: Income Tax Rate	<u>6%</u>	<u>34%</u>
Income Tax Expense	<u>\$ 18,063</u>	<u>\$ 96,218</u>

Summary. As shown in Table III below, the Commission finds that WSKY's pro forma net income at present rates is \$188,505.

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF WATER SERVICE)	
CORPORATION OF KENTUCKY FOR AN)	CASE NO. 2010-00476
ADJUSTMENT OF RATES)	

O R D E R

Water Service Corporation of Kentucky ("WSKY") has applied to adjust its rates for water service to produce additional revenues from water sales of \$448,723, or 22 percent above normalized revenues from such sales. By this Order, the Commission establishes rates that will produce additional annual revenues of \$68,898. For a customer who uses 5,000 gallons of water monthly, these rates will result in an increase of \$0.70 in his monthly bill if he resides in Bell County or \$1.15 if he resides in Hickman County.

BACKGROUND

WSKY, a Kentucky corporation, owns and operates facilities that treat and distribute water to approximately 7,376 customers in Hickman and Bell Counties, Kentucky.¹ WSKY is a wholly-owned subsidiary of Utilities, Inc. ("UI"), an Illinois corporation that indirectly owns over 70 water and wastewater systems in 15 states throughout the United States. Water Service Corporation, an Illinois corporation that is also a wholly-owned subsidiary of UI, provides various management, administrative,

¹ *Annual Report of WSKY Corporation of Kentucky to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2010* ("2010 Annual Report") at 5 and 30.

Table I: Income Tax		
Account Titles	Revenues & Expenses	Taxes
<u>OPERATING REVENUES</u>		
Operating Revenues	\$ 2,101,576	
<u>OPERATING EXPENSES</u>		
Maintenance Expenses	\$ 1,368,284	
Depreciation	206,857	
General Taxes	146,279	
Exp. Reduction - Clinton Sewer	(102,216)	
Amortization CIAC & AIAC	+ (4,350)	
Total Operating Expenses	\$ 1,614,854	
State Taxable Income before Interest Exp.	\$ 486,722	
Less: Interest Expense	- 178,169	
State Taxable Income	\$ 308,553	
Multiplied by: State Income Rate	x 6%	
Total State Income Tax Exp.		\$ 18,513
State Taxable Income	\$ 308,553	
Less: State Income Tax Exp.	- 18,513	
Federal Taxable Income	\$ 290,040	
Federal Tax Rate	x 35.00%	
Total Federal Tax Exp.		+ 101,514
Total Income Tax		\$ 120,027

Based on the accepted adjustments to operating revenues and expenses, the Commission finds WSKY's net operating income at present rates to be \$366,695 as shown in Table II.

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF WATER SERVICE)	
CORPORATION OF KENTUCKY FOR AN)	CASE NO. 2008-00563
ADJUSTMENT OF RATES)	

O R D E R

Water Service Corporation of Kentucky (“Water Service”) filed an application requesting approval to increase its water rates, to establish several new nonrecurring charges, and to make changes to certain existing nonrecurring charges. Water Service proposes to adjust its water rates to increase its operating revenues from \$1,631,079 to \$2,438,085, an increase of 50.08 percent increase or \$807,006.¹ By this Order, the Commission modifies the proposed tap-on fee, approves the remaining nonrecurring charges, and establishes water rates that will produce annual revenues of \$2,104,261. The increase will impact a customer’s monthly bill, using an average of 5,000 gallons, in Middlesboro by \$5.12 (from \$17.58 to \$22.70) and in Clinton by \$8.54 (from \$29.46 to \$38.00).

BACKGROUND

Water Service, a Kentucky corporation, is a utility subject to Commission jurisdiction.² It owns and operates facilities that treat and distribute water to

¹ Application, Exhibit 9, Calculation of Revenue Requirement (filed Mar. 5, 2009).

² KRS 278.010(3)(d).

Table III: Income Taxes		
Account Titles	Amount	Taxes
Operating Revenues	\$ 1,667,169	
<u>Operating Expenses and Interest Expense:</u>		
Operation and Maintenance Expenses	\$ 1,436,049	
Depreciation & Amortization	210,240	
CIAC Amortization	(3,181)	
General Taxes	77,928	
Interest Expense	191,409	
Total Expenses Net of Income Taxes	\$ 1,912,445	
State Taxable Income	\$ (245,276)	
Multiplied by the State Tax Rate ⁶²	6.00%	
State Income Tax	\$ (14,717)	\$ (14,717)
Federal Taxable Income	\$ (230,559)	
Multiplied by the Federal Tax Rate	34.00%	
Federal Income Tax	\$ (78,390)	(78,390)
Total Income Taxes		\$ (93,107)

Interest Expense. To reflect interest synchronization, Water Service proposed a pro forma interest expense of \$214,217 based on forecasted rate base and weighted cost of debt. The Commission has recalculated this expense to be \$191,352⁶³ based on the rate base and weighted cost of debt found reasonable herein.

Based on the aforementioned adjustments to Water Service's pro forma revenues and expenses, the Commission has determined Water Service's pro forma net operating income at present rates to be \$174,681 as shown in Table IV.

⁶² The Commission's past practice has been to use the highest tax rate applicable. Citing KRS 141.040(1), Water Service claimed that the applicable state tax was a graduated rate from 4% to 8%. The tax rates identified by Water Service, however, were for tax years 1990 through 2004. KRS 141.040(3). The tax rate for tax years beginning on or after January 1, 2007 ranges from 4% to 6%. KRS 141.040(6).

⁶³ \$5,484,135 (Commission Approved Rate Base) x 3.4892% (Commission Approved Weighted Cost of Debt) = \$191,352.