Staff DR 2-1:

Based on the calculation below, LFUCG's audit reports indicate that, for each of the past three years, the Sanitary Sewer System Business-Type Activity performed by LFUCG has had a positive cash-basis income. If LFUCG has had a positive cash-basis income, explain why LFUCG proposed an increase in sewer service and tap-on fees charged to Jessamine-South Elkhorn Water District. If the cash-basis income has not been positive, provide supporting documentation to reflect that the cash-basis income has not been positive.

Year	2019	2020	2021
Net Income before Contributions	$ 14,611,395	$ 12,540,237	$ 6,902,619
Pension / OPEB Non-Cash Adjustments	2,515,033	2,519,665	2,545,571
Subtract: Principal Payments ( )	(7,921,901)	(10,482,732)	(11,212,512)
Adjusted Net Income / (Loss)	$ 9,204,527	$ 4,577,170	$ (1,764,322)
Add: Depreciation Expense	12,517,562	13,649,916	16,327,030
Cash Basis Income	$ 30,926,616	$ 22,804,256	$ 12,798,386

<u>Response</u>: As the LFUCG audit report indicates, the Sanitary Sewer System Business-Type Activity has had a positive cash-basis income. However, the operating expenses for the fund continue to outpace revenue growth and generally outpace the CPI, which the proposed increase is based upon. An analysis of the cash basis calculation included in the Second Request for Information shows a trend of decline in cash basis income from $30.9 million in 2019 to $12.8 million in 2021. The LFUCG prepares a sewer model bi-annually that reviews historical actuals and projects future trends. This model has been audited by Causey Demgen & Moore P.C. and has served as the analytical tool used to set rates for future needs. Based on this model, the trend is expected to continue as expenses rise and the cost of constructing and maintaining equipment remains volatile due to rising inflation and supply system pressures. Looking at a 5-year history of operating expenses, as presented in the 2021 Annual Consolidated Financial Report (ACFR), expenses have increased an average of 10% in each of the past 5 years.

At a minimum, LFUCG is required to maintain 120% of the maximum annual debt service in the Sanitary Sewer Trust Fund. Additionally, our responsibility to meet Consent Decree requirements and maintain those improvements necessitates a methodical application of rate increases to meet expenses. A stable and predictable rate increase for residents reduces the risk of large, unanticipated spikes that we feel would create unnecessary challenges for households and our large customers including JSEWD. This rate is the same as that borne by the residents of Fayette County.

As noted in the 2021 ACFR, "The sanitary sewer capital construction component of the Consent Decree consists of 115 capital improvement projects intended to rehabilitate the sanitary sewer system to prevent recurring sanitary sewer overflows and unpermitted bypasses. The cost estimate for all the Remedial Measures Plan (1Uv1P) capital projects is $591 million, and LFUCG must complete the projects by December 31, 2026. As of September 2021, a total of 61 RMP projects have been completed and another 23 are in the design / construction phase, totaling approximately $311 million in capital expenditures. Generally projections show total RMP capital project expenses trending below the original estimated expenditure for the projects completed or are under construction to date. LFUCG will continue to closely monitor this trend as the overall project scope has now begun to transition away from the storage tank projects and into the pipeline upgrade projects-schedules of which are being adversely impacted by serious pipe supply shortages and price increases."

Witness: Erin Hensley

Staff DR 2-2:

Refer to LFUCG's response to Commission Staff's First Request for Information, Item 1-2, 2021 Audit Report. Provide a set of financial statements broken down by Business-Type Activity similar to those shown on pages 49-52 of the 2021 Audit Report for the fiscal year ended June 30, 2022.

Response: LFUCG is currently in the process of closing the FY22 fiscal year. The audited financial statements are typically complete and presented in January at the Budget, Finance and Economic Development Committee.

Witness: Erin Hensley

Staff DR 2-3:

Refer to Appendix B of the Commission's June 24, 2022 Order in this proceeding, which consists of an email exchange between David Barberie and Commission Staff. In the email sent on June 1, 2022, Item 5, Mr. Barberie stated "[w]ith respect to this year, both LFUCG's overall historical costs, and the costs experienced this last fiscal year justify the rate increases at least in the amount filed with the PSC." Provide support illustrating how the historical costs and actual costs experienced in the last fiscal year support the proposed rate increases.

Response: As previously discussed in response to Item 1 above, the average increase in expenses over the last 5 years was 10%. A significant increase can be observed in the 2019 fiscal year with a heavy capital investment (an additional 55-million-dollar bond issuance) related to the Consent Decree referenced above.

The FY2023 operating budget was adopted at $69,705,518 up from $67,056,285 in the prior year but doesn't represent the true costs if the city was able to adequately staff our operations. A 5% increase in salaries for FY23 as well as a mid-year application of an additional 3% for employees in FY22 is offset by increased attrition. Other notable cost increases include utilities and fuel charges which are most heavily experienced in this field.

Historically, LFUCG has been able to cash flow capital projects, alleviating its customers of interest costs associated with bonding. The current construction budget – which is in addition to the $69,705,518 above – is $46,730,000 and will further reduce cash balances. It should also be noted that capital project costs are continuing to rise in cost and may exceed the budgeted capital allowance. As noted in the 2021 ACFR, current capital projects are now principally pipeline upgrade projects, and costs are adversely impacted by supply shortages and price increases.

Witness: Erin Hensley