

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF MADISON COUNTY UTILITY)
DISTRICT FOR A CERTIFICATE OF PUBLIC)
CONVENIENCE AND NECESSITY TO CONSTRUCT) CASE NO.
A WATER STORAGE TANK AND A GENERAL) 2008-00182
RATE INCREASE TO FINANCE WATER STORAGE)
TANK)

ORDER

On May 22, 2008, Madison County Utility District ("Madison District") applied for a Certificate of Public Convenience and Necessity ("Certificate") to construct a \$1,286,310 waterworks improvement project, for authority to enter into a loan agreement with the Kentucky Infrastructure Authority ("KIA") for \$1,105,016, and for authority to increase its water rates. Because of filing deficiencies, the Commission did not accept the application for filing until July 21, 2008. On August 27, 2008, the Commission granted the Certificate and authorized Madison District to enter the proposed KIA loan.

Commission Staff, having performed a limited financial review of Madison District'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 about Staff's findings and recommendations or requests for a hearing or an informal conference no later than 14 days from the date of this Order.

IT IS THEREFORE ORDERED that:

1. All parties shall have 14 days from the date of this Order to submit to the Commission written comments, if any, regarding the attached Staff Report and to request a hearing or an informal conference in this matter.

2. Any party requesting a hearing in this matter shall state in its request its objections to the findings set forth in the Staff Report and provide a brief summary of testimony that it would present at hearing.


3. A party's failure to object to a finding or recommendation contained in the Staff Report within 14 days of this Order shall be deemed as agreement with that finding or recommendation.

4. If no request for a hearing or an informal conference is received within 14 days of this Order, this case shall stand submitted to the Commission for decision.

Done at Frankfort, Kentucky, this 5th day of February, 2009.

By the Commission

ATTEST:


Executive Director

Case No. 2008-00182

STAFF REPORT
ON
MADISON DISTRICT COUNTY UTILITY DISTRICT
CASE NO. 2008-00182

Madison County Utility District ("Madison District") applied for a Certificate of Public Convenience and Necessity ("Certificate"), for authority to enter into a loan agreement with the Kentucky Infrastructure Authority ("KIA"), and for authority to increase its water rates. In its August 27, 2008 Order, the Commission granted Madison District's Certificate and authorized the KIA loan. This Staff Report addresses the proposed increase in water rates.

To evaluate the requested increase, Commission Staff performed a limited financial review of Madison District's test-period operations. In its application, Madison District includes the report of its audit for the period ending December 31, 2006¹ and the Monthly Managerial Reports for the calendar year 2007.² Given the confusion about which test period Madison District proposes to use and the date of its Application, Staff has used the calendar year ending December 31, 2007 as the test period to determine the reasonableness of Madison District's rates.

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.

¹ Application, Exhibit H, Financial Statements and Independent Auditor's Report for the Year Ended December 31, 2006.

² Id. Exhibit I, Monthly Managerial Reports.

Mark Frost and Jason Green of the Commission's Division of Financial Analysis performed the limited review. This report summarizes Staff's findings and recommendations. Mr. Green calculated the pro forma revenue adjustment using billing information supplied by Madison District and is responsible for all findings and recommendations related to Madison District's proposed rates. Mr. Frost is responsible for all pro forma expense adjustments and the revenue requirement determination.

Madison District did not propose any pro forma adjustments other than to reflect the debt service for the proposed KIA loan and KIA's required replacement reserve. Based upon the recommendations and findings of Staff's limited review and the operating revenues and expenses reported in the 2007 Annual Report, Madison District's pro forma operating statement would appear as set forth in Appendix A.

Madison District currently has two long-term debt issuances outstanding: a 2007 KIA loan; and a Series 2008, Revenue and Refunding Bond Issuance. Using the amortization schedules³ for the outstanding and proposed long-term debt, Staff calculates a 3-year average debt service payment of \$571,275 as shown in Table 1 below.

Table 1: Average Debt Service Payment				
Series	2009	2010	2011	Totals
KIA Loan #F02-07	\$ 182,460	\$ 182,460	\$ 182,460	\$ 547,380
Revenue & Refunding Bonds, Series 2008	326,913	325,988	329,838	982,739
DWSRF Loan - Proposed	55,668	55,668	55,668	167,004
DWSRF Additional Loan - Proposed	5,567	5,567	5,567	16,701
Totals	<u>\$ 570,608</u>	<u>\$ 569,683</u>	<u>\$ 573,533</u>	\$ 1,713,824
Divide by: 3 Years				÷ 3
3 Year Average Debt Service				\$ 571,275

³ Madison District's Response to the Commission Staff's Second Information Request, Item 7(a).

In its application, Madison District requests an increase in rates that will produce additional operating revenues from water sales of \$88,860.⁴ However, by applying Madison District's requested rates to its billing analysis, Staff determined that Madison District is actually requesting a revenue requirement from rates of \$3,595,928, an increase of \$86,265 or 2.46 percent over Staff's normalized revenue from rates of \$3,509,663.

As shown in Table 2 below, Staff's recommended pro forma operations, annual debt service of \$571,275 and the appropriate debt service coverage ("DSC"),⁵ results in a revenue requirement from rates of \$3,883,245, an increase of \$373,582 or 10.64 percent over Staff's normalized revenue from rates of \$3,509,663.

	Debt Service	x	Coverage	=	Revenue Requirement
Debt Service Coverage - KIA	\$ 182,460	x	0.1	=	\$ 18,246
Debt Service Coverage - Bonds, Series 2008	\$ 327,579	x	0.2	=	65,516
Debt Service Coverage - Proposed KIA DWSRF Loan	\$ 61,235	x	0.1		6,123
Recommended Debt Service Coverage					\$ 83,762
Add: Debt Service - Total					571,275
Pro Forma Operating Expenses					2,928,904
Depreciation					444,597
Amortization					10,701
Taxes Other Than Income					48,894
Total Revenue Requirement					\$ 4,088,132
Less: Other Income & Deductions					92,411
Revenue Requirement from Operations					\$ 3,995,721
Less: Other Operating Revenues					112,477
Revenue Requirement from Water Sales					\$ 3,883,245
Less: Pro Forma Revenue - Water Sales					3,509,663
Recommended Increase – Revenue Water Sales					\$ 373,582
Percentage Increase					10.64%

⁴ Application, Exhibit E, Rate Increase Determination. \$61,097 (Estimated Annual Debt Service) + \$2,763 (Administrative Fee) + \$25,000 (KIA Required Replacement Reserve) = \$88,860.

⁵ A DSC of 1.2x for the Bonds and a DSC of 1.1x for the KIA loans.

Staff finds that Madison District's requested revenue requirement will produce a positive cash flow of \$167,981,⁶ and is sufficient to pay the pro forma "cash" expenses and meet the debt service requirements of the long-term debt issuances. Therefore, Staff recommends the Commission allow Madison District to increase its water rates to a level that will generate the requested revenue requirement of \$3,595,928. Should Madison District desire rates that will generate revenues of \$3,883,245, a level of revenue that staff finds reasonable, it should amend its application to request the rates set forth in Appendix C and provide documentary evidence to the Commission that it has published notice of those rates pursuant to 807 KAR 5:011, Section 8.

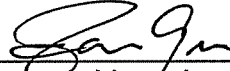
Staff recommends that the Commission approve Madison District's requested rates, which are set forth in Appendix B. Staff states that the rates contained in Appendix C will produce the recommended revenue requirement of \$3,883,245.

⁶ Revenue Requirement - Water Sales	\$ 3,595,928
Add: Other Operating Revenues	112,477
Other Income & Deductions	92,411
Total Revenue Requirement	<u>\$ 3,800,816</u>
Less: Operating Expenses	3,433,096
Net Operating Income	<u>\$ 367,720</u>
Add: Depreciation & Amortization	455,298
Sub-total	<u>\$ 823,018</u>
Less: Debt Service	655,037
Net Cash Flow	<u><u>\$ 167,981</u></u>

Signatures



Prepared by: Mark C. Frost
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

APPENDIX A
STAFF REPORT CASE NO. 2008-00182
STAFF'S RECOMMENDED
PRO FORMA INCOME STATEMENT

	Test-Period Operations	Pro Forma Adjustments	Adj. Ref	Pro Forma Operations
Operating Revenues:				
Revenues - Metered Water Sales	\$ 3,409,305	\$ 100,358	(a)	\$ 3,509,663
Fire Protection Revenue	1,260	0		1,260
Revenues - Sales of Water	<u>\$ 3,410,565</u>	<u>\$ 100,358</u>		<u>\$ 3,510,923</u>
Other Operating Revenues:				
Forfeited Discounts	\$ 73,332	0		\$ 73,332
Miscellaneous Service Revenues	37,885	0		37,885
Total Other Operating Revenues	<u>\$ 111,217</u>	<u>0</u>		<u>111,217</u>
Total Operating Revenues	<u>\$ 3,521,782</u>	<u>\$ 100,358</u>		<u>\$ 3,622,140</u>
Operating Expenses:				
Operation & Maintenance:				
Salaries & Wages - Employees	\$ 590,373	\$ (70,813)	(b)	\$ 519,560
Salaries & Wages - Officers	21,355	(6,955)	(c)	14,400
Employee Pension & Benefits	120,106	5,739	(d)	125,845
Purchased Water	1,819,567	0		1,819,567
Purchased Power	41,061	0		41,061
Materials & Supplies	160,524	(5,450)	(e)	155,074
Contractual Services - Eng.	23,987	(23,987)	(f)	0
Contractual Services - Accounting	23,680	0		23,680
Contractual Services - Legal	6,079	0		6,079
Contractual Services - Water Testing	10,090	0		10,090
Contractual Services - Other	7,158	0		7,158
Rental - Building/Real. Prop.	18,215	0		18,215
Rental - Equipment	6,830	0		6,830
Transportation	40,360	0		40,360
Insurance - Vehicle	15,596	0		15,596
Insurance - Gen. Liability	33,105	0		33,105
Insurance - Worker's Compensation	13,543	0		13,543
Advertising	768	0		768
Miscellaneous	77,973	0		77,973
Total Operation & Maintenance	<u>\$ 3,030,370</u>	<u>\$ (101,466)</u>		<u>\$ 2,928,904</u>
Depreciation	399,629	44,968	(g)	444,597
Amortization	10,701	0		10,701
Taxes Other Than Income:				
Public Service Com. Assessment	5,341	0		5,341
Payroll Taxes	46,260	(2,707)	(h)	43,553
Utility Operating Expenses	<u>\$ 3,492,301</u>	<u>\$ (59,205)</u>		<u>\$ 3,433,096</u>
Net Utility Operating Income	<u>\$ 29,481</u>	<u>\$ 159,563</u>		<u>\$ 189,044</u>
Other Income & Deductions:				
Interest Income	25,648	0		25,648
Miscellaneous Nonutility Expenses	66,763	0		66,763
Total Other Income & Deductions	<u>\$ 92,411</u>	<u>\$ 0</u>		<u>\$ 92,411</u>
Net Income Available for Debt Service	<u>\$ 121,892</u>	<u>\$ 159,563</u>		<u>\$ 281,455</u>

a. Metered Water Sales. In its 2007 Annual Report, Madison District reported test-period revenue from metered water sales of \$3,409,305. Applying the current tariffed rates to the billing information supplied by Madison District, Staff determined that the pro forma operating revenue from water sales should be increased by \$100,358 to a pro forma level of \$3,509,663.

b. Salaries and Wages - Employees. Madison District reports a test-period level of salaries and wages - employees expense of \$590,373. Using Madison District's current staff level and the hourly wages that became effective on July 1, 2008, Staff calculates a pro forma salaries and wages expense of \$519,560, as shown in Table 1 below. Accordingly, Staff recommends salaries and wages expense - employees be decreased by \$70,813 to reflect its pro forma level of \$519,560.

Emp. Position	Hours Worked		Pro Forma Wage Rates as of 07/01/08		Pro Forma Salaries & Wages
	Reg.	Over.	Reg.	Over.	
	Supervisor	2,080	415.00	\$ 18.29	
Supervisor	2,080	181.00	\$ 18.29	\$ 27.44	43,010
Manager	2,080	0.00	\$ 47,000.00	N/A	47,000
Field Service	2,080	95.75	\$ 11.48	\$ 17.22	25,527
Field Service	2,080	552.55	\$ 13.04	\$ 19.56	37,931
Field Service	2,080	511.50	\$ 11.95	\$ 17.93	34,027
Field Service	2,080	425.50	\$ 10.33	\$ 15.50	28,081
Field Service	2,080	0.00	\$ 9.00	\$ 13.50	18,720
Office Mgr	2,080	114.00	\$ 14.13	\$ 21.20	31,807
Clerical	2,080	18.25	\$ 12.22	\$ 18.33	25,753
Clerical	2,080	83.00	\$ 12.42	\$ 18.63	27,380
Clerical	2,080	46.40	\$ 9.78	\$ 14.67	21,023
Clerical	2,080	223.00	\$ 9.78	\$ 14.67	23,613
Clerical	2,080	9.50	\$ 9.78	\$ 14.67	20,481
HR/Bookkeeper	2,080	7.50	\$ 13.04	\$ 19.56	27,270
Admin. Asst	2,080	0.00	\$ 10.00	\$ 15.00	20,800
Payment Clerk	2,080	29.00	\$ 8.28	\$ 12.42	17,582
Payment Clerk	2,080	104.00	\$ 9.00	\$ 13.50	20,124
Pro Forma Payroll Totals					\$ 519,560

c. Salaries and Wages - Officers. Madison District reports a test-period level of salaries and wages - officers expense of \$21,355. Using Madison District's current commissioner level and an annual Commissioner fee of \$3,600, Staff calculates a pro forma salaries and wages expense - officers of \$14,400.¹ Accordingly, Staff recommends salaries and wages expense - officers be decreased by \$6,955 to reflect its pro forma level of \$14,400.

d. Employee Pensions and Benefits. Madison District reports a test-period level of employee pensions and benefits expense of \$120,106. On July 1, 2008, the County Employees Retirement System ("CERS") employer contribution rate was decreased to 13.5 percent. Using the current employee health insurance premiums and the employer retirement contribution rate of 13.5 percent, Staff calculates a pro forma level of employee pensions and benefits expense of \$125,845. Test period employee pensions and benefits expense has been increased by \$5,739 to reflect Staff's pro forma level.

e. Materials and Supplies. Madison District reports a test-period level of materials and supplies expense of \$160,524. In reviewing the test-period invoices, Staff believes that the items listed in Table 2 below are capital expenditures. To eliminate the capital expenditures, Staff is reducing materials and supplies expense by \$5,450.

Table 2: Capital Expenditures				
Date	Check #	Vendor	Description	Amount
12/7/2007	16687	Dudley & AJ Walker	Hydrants	\$ (350)
12/7/2007	16687	Dudley & AJ Walker	Meter Tap-on's	(1,750)
12/7/2007	16687	Dudley & AJ Walker	Road Bores	(1,750)
12/7/2007	16687	Dudley & AJ Walker	Valves	(480)
4/19/2007	14863	Neil Burns	Meter Installations	(500)
6/7/2007	15014	Neil Burns	Meter Installations	(300)

¹ 4 (Commissioners) x \$3,600 = \$14,400.

8/9/2007	16311	Neil Burns	Meter Installations	(320)
Pro Forma Adjustment				\$ (5,450)

f. Contractual Services - Engineering. Madison District reports a test-period level of contractual services - engineering expense of \$23,987. In reviewing the invoices from Madison District's engineer, CMW Inc., Staff determined that the majority of the engineering services provided are either for non-recurring or capital projects. For this reason, Staff is reducing operating expense by \$23,987 to eliminate the test-period engineering costs from operating expenses.

g. Depreciation. Madison District reports a test-period depreciation expense of \$399,629. Staff recommends that depreciation expense be increased by \$44,968 to reflect (1) removal of depreciation for plant that will be fully depreciated in 2008; (2) annualization of depreciation of utility plant placed in service in 2007; (3) depreciation of the tank that the Commission certificated in this proceeding; and (4) the 2007 audit correction.²

h. Payroll Taxes. Madison District reports a test period payroll tax expense of \$46,260. Using the pro forma payroll determined reasonable herein and the current "FICA" rate of 7.65 percent, Staff calculates a pro forma payroll tax expense of \$43,553, a decrease of \$2,707 below the reported level. Accordingly, Staff proposes to decrease payroll tax expense by \$2,707.

² Madison District's Response to the Commission Staff's Second Information Request, Item 8.

APPENDIX B
STAFF REPORT CASE NO. 2008-00182
REQUESTED RATES AND CHARGES

RATES AND CHARGES

First	280	cubic feet	\$	13.66	Minimum bill
Next	720	cubic feet		4.27	per 100 cubic feet
Next	3,000	cubic feet		4.07	per 100 cubic feet
Next	8,000	cubic feet		3.89	per 100 cubic feet
Next	88,000	cubic feet		3.72	per 100 cubic feet
Over	100,000	cubic feet		3.44	per 100 cubic feet

APPENDIX C
STAFF REPORT CASE NO. 2008-00182
RATES AND CHARGES
MADISON DISTRICT COULD JUSTIFY

First	280	cubic feet	\$	14.97	Minimum bill
Next	720	cubic feet		4.68	per 100 cubic feet
Next	3,000	cubic feet		4.46	per 100 cubic feet
Next	8,000	cubic feet		4.27	per 100 cubic feet
Next	88,000	cubic feet		4.08	per 100 cubic feet
Over	100,000	cubic feet		3.77	per 100 cubic feet

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