

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF ADAIR	)	CASE NO.
COUNTY WATER DISTRICT FOR AN	)	2021-00316
ALTERNATIVE RATE ADJUSTMENT	)	

ORDER

On September 2, 2021, Adair County Water District (Adair District) filed an application with the Commission, pursuant to 807 KAR 5:076, requesting to adjust its rates for wastewater service. This application was filed pursuant to the Commission’s Order in Case No. 2020-00308.<sup>1</sup> In its application, Adair District requested rates that would increase annual wastewater sales revenues by \$151,607, or a 17.09 percent increase to pro forma present rate water sales revenues.

To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated September 23, 2021, which, among other things, required the Commission Staff (Staff) to file a report containing its findings regarding Adair District’s application. Pursuant to the September 23, 2021 Order, on December 16, 2021, Commission Staff issued a report (Staff Report) summarizing its findings regarding Adair District’s requested rate adjustment. In the Staff Report, Commission Staff found that Adair District’s adjusted test-year operations support an overall revenue requirement of

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<sup>1</sup> Case No. 2020-00308, *Electronic Application of the Adair County Water District for a Certificate of Public Convenience and Necessity to Construct a System Improvements Project and an Order Approving a Change in Rates and Authorizing the Issuance of Securities Pursuant to KRS 278.023* (filed May 14, 2020) at 9, ordering paragraph 16.

\$1,349,597 and that an annual revenue increase of \$462,274, or 52.10 percent, is necessary to generate the overall revenue requirement.<sup>2</sup>

On December 28, 2021, Adair District filed with the Commission its comments on the Staff Report. In its response, Adair District did not agree with Commission Staff's reduction of employee health and dental insurance expenses stating that Commission Staff did not consider the value of the total compensation package, labor market conditions, or the level of benefits generally provided to employees in the utility sector or among Kentucky's water utilities. However, Adair District stated that it did not wish to contest the adjustment. Adair District did note that the rates contained in the Staff Report are higher than the application because Commission Staff did not phase-in the depreciation into the revenue calculations, as proposed in the application. Adair District argued that the utility has operated well without the working capital depreciation would provide and that the utility would still have ample working capital. Adair District voiced its concern about the impact the rate increase will have on its customer base, citing the lower than median state household income in Adair District's service territory, and requested that the Commission phase-in the proposed rates over a three-year period. Provided that the recommended wastewater service rates are accepted as filed, Adair District did not request that a conference or hearing be held.<sup>3</sup>

#### LEGAL STANDARD

Alternative rate adjustment proceedings, such as this one, are governed by 807 KAR 5:076, which establishes a simplified process for small utilities to use to request

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<sup>2</sup> Staff Report at 14.

<sup>3</sup> Adair District's Response to Staff Report (filed Dec. 28, 2021).

rate adjustments, with the process designed to be less costly to the utility and to the utility ratepayers. The Commission's standard of review of a utility's request for a rate increase is well established. In accordance with KRS 278.030 and case law, Adair District is allowed to charge its customers "only 'fair, just and reasonable rates.'"<sup>4</sup> Further, Adair District bears the burden of proof to show that the proposed rate increase is just and reasonable, under KRS 278.190(3).

### BACKGROUND

Adair District is a water district organized pursuant to KRS Chapter 74. It owns and operates a wastewater distribution system through which it provides wastewater service to approximately 1,739 customers in Adair, Kentucky.<sup>5</sup> Adair District has never filed a general rate case; rather rate adjustments have occurred through 023 financing cases.<sup>6</sup>

The Commission would note that, pursuant to the filings in this case, Adair District has been doing business as "Columbia/ Adair Utilities District aka Adair County Water District," yet has filed no notice of this name change with the Commission. The Commission finds that Adair District shall file updated tariff sheets that reflect this change in name and provide written notice to the Executive Director of the Commission of the name change.

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<sup>4</sup> *City of Covington v. Public Service Commission*, 313 S.W.2d 391 (Ky. 1958); and *Pub. Serv. Comm'n v. Com. of Kentucky v. Dewit Water District*, 720 S.W.2d 725 (Ky. 1986).

<sup>5</sup> *Annual Report of Adair District to the Public Service Commission for the Calendar Year Ended December 31, 2020 (Annual Report)* at 36.

<sup>6</sup> A 023 loan is when the applicant requests Commission approval of federal funding pursuant to KRS 278.023(3). Here the application must be approved within 30 days and the Commission cannot reject the application.

## TEST PERIOD

The calendar year ended December, 2020, was used as the test year to determine the reasonableness of Adair District's existing and proposed water rates, as required by 807 KAR 5:076, Section 9.

## SUMMARY OF REVENUE AND EXPENSES

The Staff Report summarizes Adair District's pro forma income statement as follows:

	<u>2020 Annual Report</u>	<u>Pro Forma Adjustments</u>	<u>Pro Forma Operations</u>
Total Operating Revenues	\$ 677,785	\$ 209,468	\$887,253
Utility Operating Expenses	<u>1,252,471</u>	<u>(129,278)</u>	<u>1,123,193</u>
Net Utility Operating Income	(574,686)	338,746	(235,940)
Interest and Dividend Income	<u>0</u>	<u>70</u>	<u>70</u>
Total Utility Operating Income	<u>\$ (574,686)</u>	<u>\$ 338,816</u>	<u>\$ (235,870)</u>

## MODIFICATIONS TO COMMISSION STAFF'S FINDINGS

Adair District proposed adjustments to revenues and expenses to reflect current and expected operating conditions. In the Staff Report, Commission Staff proposed additional adjustments. The Commission accepts the findings contained in the Staff Report. These adjustments are discussed below.

Billing Analysis. In the Staff Report, Commission Staff recommended to accept Adair District's proposed adjustment to increase test-year revenues by \$209,468<sup>7</sup> to reflect the normalization of sales revenues of due to an increase in rates approved in

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<sup>7</sup> *Id.* at 6, Adjustment A.

Case No. 2020-00308. The Commission finds that this adjustment is a known and measurable change to Total Metered Sales, is reasonable, and should be accepted.

Salaries and Wages - Employees. In the Staff Report, Commission Staff recommended a decrease to Adair District's test-year Salaries and Wages - Employees of \$7,535<sup>8</sup> to reflect an increase in employee's salaries and wages, and the change in the number of full-time employees subsequent to the test year. In addition, the adjustment reflected the alteration to Adair District's Hourly employee's allocation between the water and wastewater divisions. The Commission finds that this adjustment is a known and measurable change to Other Water Revenues, is reasonable, and should be accepted.

Expenses Related to Meter Installations. In the Staff Report, Commission Staff recommended a decrease to Adair District's Salaries and Wages-Employees expense by \$1,200 and Materials and Supplies by \$2,800<sup>9</sup> for the expenses related to the installation of five new wastewater connections. The Commission finds that this adjustment is a known and measurable change to Materials and Supplies, is reasonable, and should be accepted.

Salaries and Wages - Officers. In the Staff Report, Commission Staff recommended a decrease to Adair District's Salaries and Wages - Officers expense by \$11,114<sup>10</sup> to reflect the change to Adair District's water to wastewater division allocation percentages. The Commission finds that this adjustment is a known and measurable change to Salaries and Wages - Officers, is reasonable, and should be accepted.

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<sup>8</sup> *Id.* at 6–7, Adjustment B.

<sup>9</sup> *Id.* at 7–8, Adjustment C.

<sup>10</sup> *Id.* at 8–9, Adjustment D.

Employee Pensions and Benefits - Retirement. In the Staff Report, Commission Staff recommended a decrease to Adair District's Employee Pensions and Benefits - Retirement Contribution of \$41,246.<sup>11</sup> The decrease is the summation of an increase to retirement contributions due to an increase in contribution percentage from 24.06 percent to 26.95 percent, and the decrease in employee's salaries and wages. The Commission finds that these adjustments are known and measurable changes to Employee Pensions and Benefits and Interest Expense, are reasonable, and should be accepted.

Employee Pensions and Benefits - Insurance. In the Staff Report, Commission Staff recommended a decrease to Adair District's Employee Pensions and Benefits of \$15,347<sup>12</sup> to reflect the adjustment of Single Health Insurance premiums paid by Adair District from 100 percent to 78 percent, Family Health Insurance premiums from 100 percent to 66 percent, and Dental and Vision Insurance from 100 percent to 60 percent. The Commission finds that this adjustment is a known and measurable change to Employee Pensions and Benefits, is reasonable, and should be accepted.

Depreciation. In the Staff Report, Commission Staff recommended a decrease to Adair District's test-year Depreciation Expense of \$56,727<sup>13</sup> to reflect the adjustment of the useful life of capital assets to the midpoint of the Operation and Maintenance (O&M) Guide for the support of Rural Water- Waste Water Systems and Rural Development (RD) Project additions. Commission Staff's adjustment did not include the proposed phase-in for Depreciation Expense over a six-year period. The Commission reject's Adair District's

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<sup>11</sup> *Id.* at 9–10, Adjustment E.

<sup>12</sup> *Id.* at 10–11, Adjustment F.

<sup>13</sup> *Id.* at 11–12, Adjustment G.

proposed phase-in of depreciation as this does not follow general ratemaking principles and finds that Commission Staff's proposed adjustment is a known and measurable change to Depreciation Expense, is reasonable, and should be accepted. However, as discussed below, although the Commission does include the Staff Report's recommended level of Depreciation Expense, it nonetheless orders a phase-in of Adair District's revenue requirement later in this Order.

Capitalization of Test-Year Water Taps. In the Staff Report, Commission Staff recommended an increase to Adair District's test-year Depreciation Expense of \$94<sup>14</sup> to reflect the capitalization of the materials and supplies associated with the installation of new water connections. The Commission finds that this adjustment is a known and measurable change to Depreciation Expense, is reasonable, and should be accepted.

Taxes other Than Income. In the Staff Report, Commission Staff recommended a decrease to Adair District's test-year Taxes other than Income Expense of \$1,403<sup>15</sup> to reflect an increase to payroll taxes due to an increase to salaries and wages when compared to the reported test-year Taxes other Than Income. The Commission finds that this adjustment is a known and measurable change to Taxes other Than Income, is reasonable, and should be accepted.

Based on the commission's findings discussed above, the following table summarizes Adair District's adjusted pro forma operations:<sup>16</sup>

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<sup>14</sup> *Id.* at 13, Adjustment H.

<sup>15</sup> *Id.* at 13, Adjustment I.

<sup>16</sup> See Appendix A for a complete pro forma.

	<u>Staff Report pro forma</u>	<u>Commission Adjustments</u>	<u>Final Pro Forma</u>
Total Operating Revenues	\$ 887,253	\$ -	\$887,253
Utility Operating Expenses	<u>1,123,193</u>	<u>-</u>	<u>1,123,193</u>
Net Utility Operating Income	(235,940)	-	(235,940)
Interest and Dividend Income	<u>70</u>	<u>-</u>	<u>70</u>
Total Utility Operating Income	<u>\$ (235,870)</u>	<u>\$ -</u>	<u>\$ (235,870)</u>

### REVENUE REQUIREMENTS

Based upon the Commission's findings and determinations herein, Adair District requires an increase in revenues of \$462,274, or 52.10 percent above pro forma present rate revenues as shown below:

Pro Forma Operating Expenses	\$ 1,123,193
Plus: Avg. Annual Principal and Interest Payments	188,670
Debt Coverage Requirement	<u>37,734</u>
Overall Revenue Requirement	1,349,597
Less: Interest and Dividend Income	<u>(70)</u>
Revenue Required From Wastewater rates	1,349,527
Revenue from Sales at Present Rates	<u>(887,253)</u>
Required Revenue Increase	<u>462,274</u>
Percentage Increase	52.10%

### RATE DESIGN

Adair District proposed an across-the-board 17.20 percent increase to its monthly wastewater rates. Adair District applied this across-the-board increase as no cost of service study (COSS) was performed. Adair District stated that a COSS was not

completed as there had not been any material change in the water system to warrant a COSS.<sup>17</sup> The Commission finds that in the absence of a COSS, the proposed across-the-board method is an appropriate and equitable method to allocate the increased cost to Adair District's customers. Based upon the revenue requirement of \$462,274, or a 52.10 percent increase, this would result in an increase of \$23.58 for a typical residential customer's monthly water bill.<sup>18</sup>

Adair District expressed its concern about a 52.10 percent increase in the average monthly bill in its response to the Staff Report. The Commission recognizes and shares Adair District's concerns regarding the impact of such an increase. However, the Commission also recognizes and stresses the importance of financial integrity and notes that depreciation reserves should be maintained as a funding source for cost recovery and recurring replacement of a utility's investment.<sup>19</sup> The Commission has allowed utilities to phase-in large rate increases as long as the revenues generated in each phase meet the debt service requirements and expenses and eventually fully fund depreciation.<sup>20</sup> The record contains no evidence that permitting Adair District to temporarily assess wastewater rates at a level lower than could be supported will result in any degradation or reduction in the quality of service that Adair District currently provides, particularly given the eventual and relatively near-term increase provided for

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<sup>17</sup> Adair District's Response to Commission Staff's First Request for Information (filed Oct. 20, 2021), Item 7.

<sup>18</sup> Staff Report at 4.

<sup>19</sup> See Case No. 2019-00041, *Electronic Investigation into Excessive Water Loss by Kentucky's Jurisdictional Water Utilities* (Ky. PSC July 30, 2021).

<sup>20</sup> See Case No. 2021-00094, *Electronic Application of Garrison-Quincy-Ky-O-Heights Water District for a Rate Adjustment Pursuant to 807 KAR 5:076* (Ky. PSC Nov. 24, 2021).

herein. Due to the absence of evidence that the quality of Adair District’s service will decline or be degraded as a result of a temporary lower level of revenue than otherwise justifiable, and in recognition of the balance required by the provision of service under KRS 278.030(2) and the impact an increase of this magnitude would have on customers, the Commission finds that a three-year phase-in of rates should be approved. Based upon the revenue requirement of \$1,349,527 determined herein, a phase in of approximately 17.37 percent the first year, followed by two annual increases of approximately 14.80 percent and 12.89 percent, respectively, will result in sufficient revenues for the provision of service on an on-going basis. The following table illustrates the impact of the average monthly residential bill:<sup>21</sup>

	Average Bill	Difference	% Difference
Current	\$45.15		
Phase 1	\$53.00	\$7.84	17.37%
Phase 2	\$60.84	\$7.84	14.80%
Phase 3	\$68.68	\$7.84	12.89%

SUMMARY

After consideration of the evidence of record and being otherwise sufficiently advised, the Commission finds that:

1. The recommendations contained in the Staff Report are supported by the evidence of record and are reasonable and should be adopted.
2. The Commission has historically used a Debt Service Coverage (DSC) method to calculate the revenue requirement for wastewater districts with outstanding long-term debt. Application of the Commission’s DSC method to Adair District’s pro forma operations results in an Overall Revenue Requirement of \$1,349,597. A revenue

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<sup>21</sup> The typical residential customers uses approximately 5,299 gallons per month.

increase of \$462,274 from wastewater service rates is necessary to generate the overall revenue requirement.

3. The wastewater service rates proposed by Adair District would produce inadequate revenues and should be denied.

4. Phase 1, Phase 2, and Phase 3 wastewater service rates set forth in Appendix B are fair, just and reasonable and should be approved.

IT IS THEREFORE ORDERED that:

1. The findings contained in the Staff Report are adopted and incorporated by reference into this Order as if fully set out herein.

2. The general wastewater service rates proposed by Adair District are denied.

3. The Phase 1 wastewater rates set forth in Appendix B to this Order are approved for services rendered by Adair District on and after the date of this Order.

4. The Phase 2 wastewater rates set forth in Appendix B to this Order are approved for services rendered by Adair District on and after one year of the date of this Order.

5. The Phase 3 wastewater rates set forth in Appendix B to this Order are approved for services rendered by Adair District on and after two years of the date of this Order.

6. One week prior to the effective date of Phase 2, and one week prior to the effective date of the Phase 3 wastewater rates, Adair District shall publish notice following the requirements of 807 KAR 5:076, Section 5. The customer notice shall contain only the rate comparison being implemented for that rate phase.

7. Within 45 days of publishing the notice required in ordering paragraph number 6, Adair District shall file proof of notice as required pursuant to 807 KAR 5:076, Section 5(3).

8. Within 20 days of the date of entry of this Order, Adair District shall file with this Commission, using the Commission's electronic Tariff Filing System, new tariff sheets reflecting the current name by which Adair District is doing business, setting forth the rates and charges approved herein and their effective date, and stating that the rates and charges were authorized by this Order.

9. Within 20 days of the date of entry of this Order, Adair District shall provide written notice to the Executive Director of the Commission of the change in utility name and current name by which Adair District is doing business.

10. This case is closed and removed from the Commission's docket.

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By the Commission



ATTEST:

  
Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 2021-00316 DATED FEB 09 2022

	Test Year	Staff Report Adjustment	Commission Adjustments	Final pro forma
Operating Revenues				
Sewage Service Revenues				
Flat Rate Revenues				
Measured Revenues	\$ 677,785	\$ 209,468		\$ 887,253
Revenues from Public Authorities				
Revenue from Other Systems				
Miscellaneous Sewage Revenues				
Total Operating Revenues	<u>\$ 677,785</u>	<u>209,468</u>		<u>\$ 887,253</u>
Operaton Expenses				
Salaries and Wages- Employees	153,019	(7,535)		146,684
		1,200		255
Rents	255			111,649
Fuel and Power Purchased for Pumping and Treatment	111,649			58,501
Chemicals	58,501			
Miscellaneous Supplies and Expenses				
Pumping System	30,369	2,800		33,169
Maintenance Expenses				
Maintenance of Pumping System	2,828			2,828
Maintenance of Other Plant Facilities	64,946			64,946
Customer Accounts Expenses				
Uncollectable Accounts	11,653			11,653
Administrative and General Expenses				
Administrative and General Salaries	39,831	(11,114)		28,717
Office Supplies and Other Expenses	11,647			11,647
Outside Services Employed	26,212			26,212
Insurance Expenses	23,451			23,451
Employee Pensions and Benefits	139,876	(41,246)		83,284
		(15,347)		1,329
Regulatory Commission Expense	1,329			7,710
Transportation Expenses	7,710			31,687
Miscellaneous General Expenses	31,687			3,698
Maintenance of General Plant	3,698			
Total Operation and Maintenance Expenses	718,661	(71,241)		647,420
Depreciation	518,989	(56,727)		462,356
		94		13,418
Taxes Other Than Income	14,821	(1,403)		
Utility Operating Expenses	<u>1,252,471</u>	<u>(129,278)</u>		<u>1,123,193</u>
Utility Operating Income	(574,686)	338,746		(235,940)
Interest and Dividend Income		70		70
Income Available to Service Debt	<u><u>\$ (574,686)</u></u>	<u><u>\$ 338,816</u></u>		<u><u>\$ (235,870)</u></u>

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 2021-00316 DATED FEB 09 2022

The following rates and charges are prescribed for the customers in the area served by Adair County Water District. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under the authority of the Commission prior to the effective date of this Order.

Monthly Wastewater Rates

Phase 1

Minimum Bill	\$	8.22	Per Customer
All Usage (based on water usage)	\$	0.00845	Per Gallon

Phase 2

Minimum Bill	\$	9.44	Per Customer
All Usage (based on water usage)	\$	0.00970	Per Gallon

Phase 3

Minimum Bill	\$	10.66	Per Customer
All Usage (based on water usage)	\$	0.01095	Per Gallon

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