

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF SOUTHERN	)	CASE NO.
MADISON WATER DISTRICT FOR A RATE	)	2022-00129
ADJUSTMENT PURSUANT TO 807 KAR 5:076	)	

NOTICE OF FILING OF COMMISSION STAFF'S REPORT

Notice is hereby given that, in accordance with the Commission's Order of September 20, 2022, the attached report containing the findings of Commission Staff regarding the Applicant's proposed rate adjustment has been filed in the record of the above-styled proceeding. Pursuant to the Commission's June 15, 2022 Order, Southern Madison Water District (Southern Madison District) is required to file written comments regarding the findings of Commission Staff no later than 14 days from the date of this report. The Commission directs Southern Madison District to the Commission's July 22, 2021 Order in Case No. 2020-00085<sup>1</sup> regarding filings with the Commission.



Linda C. Bridwell, PE  
Executive Director  
Public Service Commission  
P.O. Box 615  
Frankfort, KY 40602

DATED OCT 05 2022

cc: Parties of Record

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<sup>1</sup> Case No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19* (Ky. PSC July 22, 2021), Order (in which the Commission ordered that for case filings made on and after March 16, 2020, filers are NOT required to file the original physical copies of the filings required by 807 KAR 5:001, Section 8).

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COMMISSION STAFF'S REPORT ON  
SOUTHERN MADISON WATER DISTRICT

Southern Madison Water District (Southern Madison District) is a water utility organized pursuant to KRS Chapter 74 that owns and operates a water distribution system through which it provides retail water service to approximately 5,222 residential customers, 108 commercial customers, 13 industrial customers, and 8 public authorities that reside in Garrard and Madison counties, Kentucky.<sup>1</sup> On May 24, 2022, Southern Madison District filed an application, pursuant to 807 KAR 5:076. To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated June 15, 2022. On September 20, 2022, the Commission, on its own motion, found that additional time was necessary for Commission Staff to review and produce an accurate report and, by Order dated September 20, 2022, amended the procedural schedule to extend the date of the Commission Staff Report to October 5, 2022. Southern Madison District responded to two rounds of discovery. There are no intervenors in this matter. This is Southern Madison District's first general base rate adjustment according to Commission Record.

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<sup>1</sup> *Annual Report of Southern Madison Water District to the Public Service Commission (Annual Report) for the Calendar Year Ended December 31, 2020 (2020 Annual Report) at 12 and 49.*

Commission Staff notes that Southern Madison District's 2020 Annual Report reported a water loss of 26.58 percent.<sup>2</sup> Commission regulation 807 KAR 5:066(6)(3) states that for ratemaking purposes, a utility's water loss shall not exceed 15 percent of total water produced and purchased, excluding water consumed by a utility in its own operations. At a 26.58 percent water loss, the annual cost to Southern Madison District of water above the allowable 15 percent is \$128,144<sup>3</sup> while the annual cost of total water loss is \$294,134.<sup>4</sup>

To comply with the requirements of 807 KAR 5:076, Section 9,<sup>5</sup> Southern Madison District used the calendar year ended December 31, 2020, as the basis for its application. Using its pro forma test-year operations, Southern Madison District determined that a revenue increase of \$70,972, or 3.82 percent was necessary, as shown in the calculation below.

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<sup>2</sup> Annual Report at 57.

<sup>3</sup>

	Purchased Water	Purchased Power	Total
2021 Pro Forma Expenses	\$ 1,068,505	\$ 38,093	\$ 1,106,598
Multiplied by: Water Loss in Excess of 15 Percent	11.58%	11.58%	11.58%
Excess Cost	<u>\$ 123,733</u>	<u>\$ 4,411</u>	<u>\$ 128,144</u>

<sup>4</sup>

	Purchased Water	Purchased Power	Total
2021 Pro Forma Expenses	\$ 1,068,505	\$ 38,093	\$ 1,106,598
Multiplied by: Total Water Loss	26.58%	26.58%	26.58%
Excess Cost	<u>\$ 284,009</u>	<u>\$ 10,125</u>	<u>\$ 294,134</u>

<sup>5</sup> The reasonableness of the proposed rates shall be determined using a 12-month historical test period, adjusted for known and measurable changes that coincides with the reporting period of the applicant's annual report for the immediate past year.

	Southern Madison District
Pro Forma Operating Expenses	\$ 1,946,228
Less: Interest Income	(15,428)
Revenue Requirement - Water Rates	1,930,800
Less: Normalized Revenue from Service	(1,859,828)
Required Revenue Increase	<u>\$ 70,972</u>
Percent Increase	<u>3.82%</u>

To determine the reasonableness of the increase proposed by Southern Madison District, Commission Staff performed a limited financial review of Southern Madison District's test-year operations. The scope of Commission Staff's review was limited to determining whether operations reported for the test year were representative of normal operations. Known and measurable<sup>6</sup> changes to test-year operations were identified and adjustments made when their effects were deemed material. Insignificant and immaterial discrepancies were not necessarily pursued or addressed.

Commission Staff's findings are summarized in this report. Travis Leach reviewed the calculation of Southern Madison District's Overall Revenue Requirement. Elizabeth Stefanski reviewed Southern Madison District's reported revenues and rate design.

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<sup>6</sup> Commission regulation 807 KAR 5:076, Section 9, sets the standard for the determination of the reasonableness of proposed rates and states, in pertinent part, that the test period shall be "adjusted for known and measurable changes." See also Case No. 2001-00211, *The Application of Hardin County Utilities District No. 1 for (1) Issuance of Certificate of Public Convenience and Necessity; (2) Authorization to Borrow Funds and to Issue its Evidence of Indebtedness Therefore; (3) Authority to Adjust Rates; and (4) Approval to Revise and Adjust Tariff* (Ky. PSC Mar. 1, 2002); Case No. 2002-00105, *Application of Northern Kentucky Utilities District for (A) an Adjustment of Rates; (B) a Certificate of Public Convenience and Necessity for Improvements to Water Facilities if Necessary; and (C) Issuance of Bonds* (Ky. PSC June 25, 2003); and Case No. 2017-00417, *Electronic Proposed Adjustment of the Wholesale Water Service Rates of Lebanon Water Works* (Ky. PSC July 12, 2018).

## SUMMARY OF FINDINGS

1. Overall Revenue Requirement and Required Revenue Increase. By applying the Operating Ratio method, as generally accepted by the Commission, Commission Staff found that Southern Madison District's required revenue from rates is \$2,285,448 to meet the Overall Revenue Requirement of \$2,330,218, and that a \$424,983 revenue increase, or 22.84 percent, to pro forma present rate revenues is necessary to generate the Overall Revenue Requirement.

2. Monthly Water Service Rates. Southern Madison District proposed to increase its monthly retail water service rates by approximately 3.82 percent across the board.<sup>7</sup> Southern Madison District has not performed a cost of service study (COSS). Southern Madison District stated that it did not complete a COSS as there has been no material changes in the water system.<sup>8</sup>

The Commission has previously found that in the absence of a COSS, the allocation of a revenue increase applied in the absence of a COSS evenly across the board to a utility's rate design is appropriate when there has been no evidence entered into the record demonstrating that this method is unreasonable. Finding no such evidence in this case, Commission Staff has followed the method previously accepted by the Commission and has allocated the \$424,983 revenue increase evenly across the board to Southern Madison District's monthly retail and wholesale water service rates.

The rates set forth in Appendix A to this report are based upon the revenue requirement, as calculated by Commission Staff, and will produce sufficient revenues

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<sup>7</sup> Application, Attachment 3, Current and Proposed Rates.

<sup>8</sup> Southern Madison Water District's Responses to Commission Staff's First Request for Information (Staff's First Request) (filed July 15, 2022), Item 4.

from water sales to recover the \$2,285,448 Revenue Required from Rates, an approximate 22.84 percent increase. These rates, including the water loss recovery surcharge of \$1.94, will increase a typical residential customer's monthly water bill from \$26.30 to \$34.23, an increase of \$7.93, or approximately 30.15 percent.<sup>9</sup> The increase in a typical customer's monthly water bill before the water loss recovery surcharge, is from \$26.30 to \$32.29, an increase of \$5.99 or 22.78 percent.

3. Nonrecurring Charges. Following the Commission's recent decisions,<sup>10</sup> Commission Staff has reviewed Southern Madison District's nonrecurring charges. The Commission found that as district personnel are currently paid during normal business hours, estimated labor costs previously included in determining the amount of Nonrecurring Charges should be eliminated from the charges. Commission Staff has reviewed the cost justification information provided by Southern Madison District and have adjusted these charges by removing Field Labor Costs and Office/Clerical Labor Costs from those charges that occur during normal business hours.<sup>11</sup> Southern Madison District also provided information about the Returned Check Charge,<sup>12</sup> to which Commission Staff adjusted the charge to \$0.75 for the office supplies, as Southern

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<sup>9</sup>  $\$34.23$  [ $\$32.29$  (Average Bill New Water Rates) +  $\$1.94$  (Water Loss Reduction Surcharge)] -  $\$26.30$  (Average Bill Current Water Rates) =  $\$7.93$  (Total Difference in Customer Bill)  $\div$   $\$26.30$  (Average Bill Current Water Rates) = 30.15%.

<sup>10</sup> Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020) and Case No. 2020-00167, *Electronic Application of Ohio County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 3, 2020), Case No. 2020-00196, *Electronic Application of West Daviess County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020), and Case No. 2020-00195 *Electronic Application of Southeast Daviess County Water District for an Alternative Rate Adjustment*, (Ky. PSC Dec. 30, 2020).

<sup>11</sup> Southern Madison District's Response to Staff's First Request, Item 8.

<sup>12</sup> Southern Madison District's Response to Staff's First Request, Item 8.

Madison District's bank does not charge a fee for a returned check. Such adjustments result in the following revised nonrecurring charges:

Nonrecurring Charges

Late Payment Charge	10%
Connection/Turn On Charge	\$15.50
Field Collection Charge	\$15.50
Meter Re-read Charge	\$15.50
Service Call / Investigation	\$15.50
5/8" x 3/4" Meter Test Charge	\$15.50
1 1/2" Meter Test Charge or larger	Actual
Turn On Charge - After hours	\$51.00
Field Collection Charge – After hours	\$51.00
Meter Re-read – After hours	\$51.00
Service Call - After hours	\$51.00
Return Check Charge	\$0.75
Meter Relocation Charge	Actual
Damage to Meter Equipment	Actual

The adjustments to the Nonrecurring Charges results in a decrease to the charges and an increase to the total revenue requirement of \$19,658 as shown below. Commission Staff recommends that Southern Madison District should be ordered to adjust its nonrecurring charges to those found in the Appendix to this report.

Other Water Revenues	Num.	Current Rate	Total	Revised Rate	Adj.	Pro Forma
Late Payment Charge		10%				-
Connection Turn-On Charge	725	\$30.00	\$29,950	\$15.50	(\$18,712)	\$11,238
Field Collection Charges	0	\$30.00	-	\$15.50		-
Meter Re-read Charge	0	\$30.00	-	\$15.50		-
Service Call/Investigation	0	\$30.00	-	\$15.50		-
Meter Test (5/8 x 3/4)	0	\$56.00	-	\$15.50		-
Meter Test (1 1/2 or larger)	0	Actual	-	Actual	-	-
Turn On Charge After hours	0	\$38.50	-	\$51.00		-
Field Collection - After hours	0	\$38.50	-	\$51.00		-
Meter Re-read After hours	0	\$38.50	-	\$51.00		-
Service Call - After hours	0	\$38.50	-	\$51.00		-
Returned Check Charge	39	\$25.00	\$975	\$0.75	(\$946)	\$29.00
Meter Relocation Charge	0	Actual	-	Actual	-	-
Damage to Meter Equipment	0	Actual	-	Actual	-	-

\$30,925

(\$19,658)

\$11,267

4. Request for Surcharge. Southern Madison District requested the Commission authorize a water loss reduction surcharge of \$1.94 per customer per month over a 48 month duration to assist in lowering system water loss to more acceptable levels.<sup>13</sup> No formal plan or explanation was given by Southern Madison District that indicated any specific future use of the surcharge funds. Commission Staff recalculated the monthly per customer impact of the water loss adjustment and believes the \$1.94 surcharge proposed by Southern Madison District is a materially accurate representation of the per customer impact on the actual annual cost of water loss above 15 percent. The use of a surcharge is consistent with prior Commission action in cases involving water utilities with excessive unaccounted-for water loss in excess of 30 percent.<sup>14</sup> The Commission has also ordered surcharges even when a utility has not specifically requested a surcharge.<sup>15</sup> Recently, the Commission has allowed water utilities with reported water loss above the 15 percent threshold to assess water loss reduction surcharges.<sup>16</sup>

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<sup>13</sup> Application, Attachment 2, Reasons for Application.

<sup>14</sup> See Case No. 96-126, *An Investigation into the Operations and Management of South Woodford Water District* (Ky. PSC Aug. 11, 1997); Case No. 2011-00217, *Application of Cannonsburg Water District for (1) Approval of Emergency Rate Relief and (2) Approval of the Increase in Nonrecurring Charges*, (Ky. PSC June 4, 2012); Case No. 2018-00017, *Application of Martin County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 5, 2018); Case No. 2018-00429, *Application of Graves County Water District for an Alternative Rate Adjustment* (Ky. PSC Sept. 30, 2019); and Case No. 2019-00119, *Electronic Application of Estill County Water District No. 1 for a Surcharge to Finance Water Loss Control Efforts* (Ky. PSC Mar. 24, 2010); Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020), Order at 11-13.

<sup>15</sup> Case No. 2020-00311, *Electronic Application of Cawood Water District for an Alternative Rate Adjustment* (Ky. PSC Apr. 8, 2021), Order at 3.

<sup>16</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).



Recognizing prior Commission precedent to allow the use of surcharges to assist utilities in obtaining the proper funding needed to combat water loss, Commission Staff recommends the Commission approve Southern Madison District's request and authorize the surcharge for a temporary period of 48 months, with a review of the necessity to continue the surcharge before the temporary period expires. Commission Staff also recommends the Commission establish a separate proceeding to monitor the surcharge and place strict controls over the use of the funds that will be collected from the surcharge. Further, Commission Staff recommends the Commission require Southern Madison District to develop a long-term plan to address its aging infrastructure and combat water loss within six months of the final order in this proceeding.

#### PRO FORMA OPERATING STATEMENT

Southern Madison District's Pro Forma Operating Statement for the test year ended December 31, 2020, as determined by Commission Staff, appears below.

	Test Year	Adjustment	Reference	Pro Forma
<b>Operating Revenues</b>				
Total Metered Sales	\$ 1,895,469	\$ (9,193)	A	
		\$ (30,925)	A	
		5,114	A	\$ 1,860,465
<b>Other Water Revenues</b>				
Forfeited Discounts	-	18,075	B	18,075
Misc Service Revenues	-	11,267	C	11,267
<b>Total Operating Revenues</b>	<b>1,895,469</b>	<b>(5,662)</b>		<b>1,889,807</b>
<b>Operating Expenses</b>				
<b>Operation and Maintenance Expenses</b>				
Salaries and Wages - Employees	330,112	46,558	D	
		(20,955)	E	355,715
Salaries and Wages - Officers	13,421	979	F	14,400
Employee Pensions and Benefits	227,094	(78,440)	G	148,654
Purchased Water	1,068,505	(123,733)	H	944,772
Purchased Power	38,093	(4,411)	H	33,682
Materials and Supplies	174,806	(48,895)	E	125,911
Contractual Services - Accounting	11,424	10,791	I	22,215
Contractual Services - Other	7,200	1,250	I	8,450
Insurance - General Liability	20,248			20,248
Insurance - Other	27,594	(23,161)	J	4,433
Miscellaneous Expenses	72,413	12,000	K	
		23,161	J	107,574
<b>Total Operation and Maintenance Expenses</b>	<b>1,990,910</b>	<b>(204,856)</b>		<b>1,786,054</b>
Depreciation Expense	229,388	3,486	L	
		1,746	E	234,620
Taxes Other Than Income	24,832	5,086	D	29,918
<b>Total Operating Expenses</b>	<b>2,245,130</b>	<b>(196,284)</b>		<b>2,050,592</b>
<b>Utility Operating Income(Loss)</b>	<b>\$ (349,661)</b>	<b>\$ 190,622</b>		<b>\$ (159,039)</b>

A. Billing Analysis. Southern Madison District made an adjustment of (\$8,828) to Metered Water Sales for leak adjustments and provided a billing analysis listing the water usage and water sales revenue for the 12-month test year in its application, with total metered water sales revenue reported as \$1,859,828.<sup>17</sup> Commission Staff calculated a normalized revenue amount based on the statistics compiled in the table below, which include net billing adjustments of (\$8,191),<sup>18</sup> which is based on the 2020

<sup>17</sup> Application, Attachment 5, 2020 Current Billing Analysis.

<sup>18</sup> Southern Madison District's Responses to Commission Staff's Second Request for Information (Staff's Second Request), Item 3 and Item 4, (filed Aug. 19, 2022).

adjustment reports for Leak Adjustments<sup>19</sup> and for mis-read meters,<sup>20</sup> equaling a normalized revenue of \$1,860,465. Commission Staff increased Retail Water Sales by \$5,114 as a billing analysis adjustment.

During the test year, Southern Madison District recorded \$9,193<sup>21</sup> in forfeited discounts as Retail Water Sales revenue. Southern Madison District also reported \$30,925 of nonrecurring charges to Retail Water Sales.<sup>22</sup> Southern Madison District reported Total Metered Water Sales of \$1,895,469 in its 2020 Annual Report.<sup>23</sup> Southern Madison District did not report any Forfeited Discount revenue or Miscellaneous Service Revenue in its 2020 Annual Report. Commission Staff reclassified the late payment charges of \$9,193 and the nonrecurring charge revenue of \$30,925 by decreasing Total Metered Sales and increasing Other Water Revenue by those amounts. The adjustment to balance the Adjusted Test Year amount and the Normalized Revenue amount is an increase to Metered Water Sales of \$5,114 as seen in the Table below.

Meter Size	Bills	Gallons Sold	Revenue
ALL	66,076	283,801,250	\$1,868,655
Less: Billing Adjustments			(\$8,191)
Normalized Revenue			<u>\$1,860,465</u>
2020 ANNUAL REPORT			\$1,895,469
Less: Misc. Service Charges			(30,925)

<sup>19</sup> Southern Madison District's Responses to Staff's Second Request, Item 3.

<sup>20</sup> Southern Madison District's Responses to Staff's Second Request, Item 4.

<sup>21</sup> Southern Madison District's Responses to Staff's First Request, Item 7.

<sup>22</sup> Southern Madison District's Responses to Staff's First Request, Item 6\_Nonrecurring\_Charges.xlsx.

<sup>23</sup> 2020 Annual Report at 49.

Less: Forfeited Discount Revenue	(9,193)
Subtotal	<u>\$1,855,351</u>
Adjustment to Retail Water Sales	\$5,114

B. Forfeited Discounts. During the test year, Southern Madison District recorded the annual amount of \$9,193<sup>24</sup> for forfeited discounts as Retail Water Sales revenue. Given that the test year occurred during the moratorium regarding the collection of late payment fees due to the COVID-19 pandemic, Commission Staff normalized the revenue from Forfeited Discounts to the 2019 level. Based upon the 2019 amount of Forfeited Discount revenue, Commission Staff increased pro forma Forfeited Discounts by \$18,075.<sup>25</sup>

C. Miscellaneous Service Revenue. As noted above, Southern Madison District did not report any Other Water Revenues in its 2020 Annual Report, the revenue collected from nonrecurring charges was reported as Metered Water Sales. Southern Madison District provided information about the nonrecurring charges revenue,<sup>26</sup> and Commission Staff calculated an adjustment to Other Water Revenue, removing labor costs as discussed above. The reclassified test year Miscellaneous Service Revenue of \$30,925 is decreased by (\$19,658), and an adjustment to Nonrecurring charges results in an increase to Other Water Revenue-Miscellaneous Service Revenue of \$11,267.

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<sup>24</sup> Southern Madison District's Responses to Staff's First Request, Item 7\_Late\_Charges.xlsx.

<sup>25</sup> Southern Madison District's Responses to Staff's First Request, Item 7\_Late\_Charges.xlsx.

<sup>26</sup> Southern Madison District's Responses to Staff's First Request, Item 8\_Non-Recurring\_Charges\_Cost\_Justification.pdf.

D. Salaries and Wages – Employees & FICA. In its application Southern Madison District’s test year Salaries and Wages – Employees Expense was \$330,112. Southern Madison District proposed an adjustment to decrease test-year Salaries and Wages – Employees Expense by \$19,782, as well as decrease FICA taxes by an associated \$1,092, citing the changes in staffing and salary levels since the test year.<sup>27</sup> To normalize new employees to test-year hours of former employees in the same position, Commission Staff determined that Salaries and Wages – Employees Expense should be increased by \$46,558 as shown below.

Employee Title	Pro Forma Hours Worked	Pro Forma Overtime Hours	Pro Form Wage Rate	Pro Forma Wages
Superintendent	N/A	N/A	\$ 65,000.00	\$ 65,000
Field Technician	2080	315	18.00	45,945
Equipment Operator	2080	127	21.00	47,681
Field Technician	2080	142	18.00	41,274
Field Technician	2080	142	15.00	34,395
Field Technician	2080	142	14.00	32,102
Customer Service	2079	66	16.38	35,676
Bookkeeper	2072	40	20.00	42,640
Customer Service	2063	45	15.00	31,958
Total Pro Forma Salaries and Wages				376,670
Less: Test Year Expense				<u>330,112</u>
Increase(Decrease) to Test Year				<u>\$ 46,558</u>

As a result of Commission Staff’s increase to Salaries and Wages – Employees, Commission Staff has made an adjustment to increase FICA Tax Expenses to reflect the adjusted payroll costs, as shown below.

Pro Forma FICA Applicable Salaries and Wages	\$ 391,070
Multiply by: FICA Rate	<u>7.65%</u>
Pro Forma FICA Taxes	29,917
Less: Test Year Payroll Taxes	<u>(24,831)</u>

<sup>27</sup> Application, Attachment #4, Reference B.

Adjustment	\$ 5,086
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E. Tap On Fees. In the test year, Southern Madison District collected \$69,850 which was associated with tap-on fees for new customers. In its application, Southern Madison District proposed an adjustment to reduce Salaries & Wage Expense – Employees by \$20,955 as well as Materials & Supplies Expense by \$48,895 to properly remove expenses related to tap-on fees.<sup>28</sup> Commission Staff agrees that the adjustments proposed by Southern Madison District are known and measurable and accurately reflect pro forma expenses and have included them in the pro forma calculation. In addition, Staff has made an adjustment to increase Depreciation Expense to reflect the recovery of expenses associated with tap-on fees in accordance with Commission Precedent, as shown below.

Test-Year Tap-On Fees	\$ 69,850
Divide By: 40 Years	40
Adjustment to Depreciation	\$ 1,746

F. Salaries and Wages – Officers. In its application, Southern Madison District proposed an adjustment to increase Salaries and Wages – Officers by \$979 to accurately annualize Commissioner Fees based on a full year of payments.<sup>29</sup> Upon review, Commission Staff agrees that the adjustment proposed by Southern Madison District is

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<sup>28</sup> Application, Attachment #4, Reference H.

<sup>29</sup> Application, Attachment #4, Reference C.

known and measurable and accurately reflects pro forma expenses and have included them in the pro forma calculation.

G. Employee Pensions and Benefits. Southern Madison District included \$227,094 in test-year Employee Benefits Expense related to insurance and retirement benefits. As part of its employee compensation, Southern Madison District pays 100 percent its employees' low-option single coverage health insurance premiums. For employees with high-option single coverage health insurance premiums, the district requires that the employee contribute \$100, or 14.8 percent, towards the monthly premium.

Commission Staff notes that the Commission has consistently made ratemaking adjustments to reduce the cost of employer-sponsored healthcare paid by some utilities when certain aspects of those benefit packages were found to be unreasonable based on a review of total salaries and fringe benefits. The Commission continues to place greater emphasis on evaluating employees' total compensation packages, including both salary and benefits programs, for market and geographic competitiveness to ensure the development of a fair, just and reasonable rate.<sup>30</sup>

As Southern Madison District's employees currently pay zero percent of their low-option single coverage health insurance premiums, Commission Staff has calculated the total pro forma allowable premiums, shown below. Commission Staff notes that only two employees currently have low-option single coverage health insurance.

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<sup>30</sup> Case 2020-00167, *Electronic Application of Ohio County Utilities District for an Alternative Rate Adjustment* (Ky. PSC Dec. 2, 2020). Case No. 2020-00296, *Electronic Application of Allen County Utilities District for an Alternative Rate Adjustment* (Ky. PSC Feb. 3, 2021).

	<u>District Contribution</u>	<u>BLS Contribution Rate</u>	<u>Reduction Adjustment</u>	<u>Pro Forma Contributions</u>
Health (Employee)	\$ 1,350	22%	\$ (297)	\$ 1,053
Pro Forma 100% Contribution Premiums			\$ 1,053	
Multiply by: 12 Months			12	
Pro Forma 100% Contribution Premiums			\$ 12,636	
Less: Test-year Premiums			<u>(13,800)</u>	
Pro Forma Adjustment			<u>\$ (1,164)</u>	

In addition to health and life insurance, Southern Madison District employees participate in Kentucky's County Employee Retirement System (CERS). As part of CERS, Southern Madison District makes contributions to employee's retirement account based on annual salaries and wages. Using the pro forma Salaries and Wages – Employees Expense discussed above, Commission Staff normalized annual contributions using the CERS rate effective July 1, 2021, of 26.95 percent as shown below.

Pro Forma Applicable Salaries and Wages	\$ 376,670
Multiply By: Pro Forma CERS Contribution Rate	<u>26.95%</u>
Pro Forma CERS Contributions	<u>\$ 101,512</u>

Considering both adjustments discussed above, Commission Staff calculated pro forma Employee Benefits Expense should be decreased by \$78,440 as shown below.

Pro Forma Health & Dental Insurance Benefits	\$ 47,142
Pro Forma Pension Contributions	<u>101,512</u>
Pro Forma Health, Dental, and Pension Benefits	148,654
Less: Test Year Pensions and Benefits	<u>(227,094)</u>



Adjustment

(78,440)

H. Water Loss. In its application, Southern Madison District proposed adjustments to Purchased Water and Purchased Power Expense of \$123,771 and \$4,413 respectively, to account for the district's unaccounted-for water loss in excess of 15 percent.<sup>31</sup> Commission Staff agrees that such adjustments are appropriate, but also notes that the amounts should be \$123,733 and \$4,411, respectively, as shown below.

I. Contractual Services. In Commission Staff's review of Southern Madison District's financial documents, it discovered that Accounting and Legal Contractual Services were understated by \$10,791 and \$1,250, respectively. To accurately represent pro forma levels of expenses, Commission Staff has made adjustments to increase Accounting and Legal Contractual Services by the amounts listed above, as calculated below.

General Ledger Accounting Contractual Services	\$ 22,215
Less: Test-Year Accounting Contractual Services	<u>(11,424)</u>
Pro Forma Adjustment	<u>\$ 10,791</u>
General Ledger Legal Contractual Services	\$ 8,450
Less: Test-Year Legal Contractual Services	<u>(7,200)</u>
Pro Forma Adjustment	<u>\$ 1,250</u>

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<sup>31</sup> Application, Attachment #4, Reference G.

J. Bank Charges Misclassification. As discussed in Adjustment L, Southern Madison District states that its Bank Charges Expense are included in Miscellaneous Expense. However, upon Commission Staff's reconciliation of the district's year end trial balance to the test-year line items, it appears that Bank Charges were mistakenly included in Insurance – Other. While the reclassification adjustment does not affect the revenue requirement, and therefore the calculation of rates, Commission Staff has nonetheless included an adjustment reducing Insurance – Other Expense by \$23,161 and increased Miscellaneous Expense by the same amount for the sake of accurately representing test-year levels of expenses.

	Purchased Water	Purchased Power	Total
2021 Pro Forma Expenses	\$ 1,068,505	\$ 38,093	\$ 1,106,598
Multiplied by: Water Loss in Excess of 15 Percent	11.58%	11.58%	11.58%
Excess Cost	<u>\$ 123,733</u>	<u>\$ 4,411</u>	<u>\$ 128,144</u>

K. Bank Charges Increase. In its application, Southern Madison District proposed an adjustment to increase Miscellaneous Expense by \$12,000 to account for an increase in Bank Charges for online payments placed into effect since the test-year.<sup>32</sup> Commission Staff agrees that such an adjustment is appropriate as it represents a known and measurable increase to test-year expense level and has therefore included it in pro forma operations.

L. Depreciation Expense. In its application, Southern Madison District included \$229,388 in Depreciation Expense and proposed to increase test-year

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<sup>32</sup> Application, Attachment #4, Reference I.

Depreciation Expense by \$3,435<sup>33</sup> citing Commission precedent of evaluating the reasonableness of the depreciation practices of small water utilities using the National Association of Regulatory Utility Commissioners' (NARUC) report titled *Depreciation Practices for Small Utilities* (NARUC Study) published in 1979. When no evidence exists to support a specific life that is outside the NARUC ranges, the Commission has historically used the midpoint of the NARUC ranges to depreciate the utility plant. In addition, Southern Madison District proposed an adjustment increasing depreciation expense by \$51 to address a minor discrepancy between the reported test-year depreciation and its asset ledger detail.<sup>34</sup>

Upon examination, Commission Staff agrees that the adjustments proposed by Southern Madison District are known and measurable and accurately reflects adjusting Southern Madison District's assets' useful life to the midpoint of the life's found in the NARUC Study and has included it in pro forma operations.

#### OVERALL REVENUE REQUIREMENT AND REQUIRED REVENUE INCREASE

In its application, Southern Madison District did not utilize either the Debt Service Coverage (DSC) or Operating Ratio method, instead opting to only recover expenses with no allowance for additional working capital or equity growth, as shown below.

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<sup>33</sup> Application, Attachment #4, Reference K.

<sup>34</sup> Application, Attachment #4, Reference J.

	<u>Southern Madison District</u>
Pro Forma Operating Expenses	\$ 1,946,228
Less: Interest Income	<u>(15,428)</u>
Revenue Requirement - Water Rates	1,930,800
Less: Normalized Revenue from Service	<u>(1,859,828)</u>
Required Revenue Increase	<u>\$ 70,972</u>
Percent Increase	<u>3.82%</u>

By applying the Operating Ratio Method, as generally accepted by the Commission, Commission Staff found Southern Madison District’s Overall Revenue Requirement to be \$2,330,218. A revenue increase of \$424,983, or 22.84 percent, is necessary to generate the Overall Revenue Requirement.

The operating ratio methodology<sup>35</sup> is used when there is no basis for a rate-of-return determination, the cost of the utility has fully or largely been funded through contributions, or there is little or no outstanding long-term debt. Since Southern Madison District does not currently have any outstanding debt, Commission Staff is of the opinion that an operating ratio of 88 percent will allow Southern Madison District sufficient revenues to cover its reasonable operating expenses and provide for reasonable equity growth. Commission Staff concludes that the Operating Ratio Method is appropriate, as the district does not currently have any outstanding debt.

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<sup>35</sup> Operating Ratio is defined as the ratio of expenses, including depreciation and taxes, to gross revenues. It is illustrated by the following equation:

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

	Commission Staff
Operating Expenses	\$ 2,050,592
Divide by: Operating Ratio	<u>88%</u>
Overall Revenue Requirement	2,330,218
Less: Other Operating Revenue	(29,342)
Interest Income	<u>(15,428)</u>
Revenue Requirement - Water Rates	2,285,448
Less: Normalized Revenue from Service	<u>(1,860,465)</u>
Required Revenue Increase	<u>\$ 424,983</u>
Percentage Increase	<u>22.84%</u>

## Signatures

/s/Travis Leach\_\_\_\_\_

Prepared by: Travis Leach  
Revenue Requirement Branch  
Division of Financial Analysis

/s/ Elizabeth Stefanski\_\_\_\_\_

Prepared by: Elizabeth Stefanski  
Rate Design Branch  
Division of Financial Analysis

APPENDIX

APPENDIX TO COMMISSION STAFF'S REPORT OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2022-00129 DATED OCT 05 2022

The following rates and charges are prescribed for the customers in the area served by Southern Madison 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 Water Rates

5/8 X 3/4-Inch Meter

First	2,000	Gallons	\$16.508	Minimum Bill
Next	1,000	Gallons	0.008138	Per Gallon
Next	3,000	Gallons	0.007635	Per Gallon
Next	4,000	Gallons	0.007070	Per Gallon
Next	15,000	Gallons	0.005999	Per Gallon
Next	25,000	Gallons	0.005630	Per Gallon
Over	50,000	Gallons	0.004955	Per Gallon
Water Loss Reduction Surcharge limited to 48 months			\$1.94	per month

Nonrecurring Charges

5/8 x 3/4 Inch Water Tap On	\$1,337
All Larger Meter sizes	Actual
Late Payment Charge	10%
Connection Turn-On Charge	\$15.50
Field Collection Charges	\$15.50
Meter Re-read Charge	\$15.50
Service Call/Investigation	\$15.50
Meter Test Charge (5/8 x 3/4)	\$15.50
Meter Test Charge (1 1/2 or larger)	Actual
Turn On Charge After hours	\$51.00
Field Collection - After hours	\$51.00
Meter Re-read After hours	\$51.00

Service Call - After hours	\$51.00
Returned Check Charge	\$0.75
Meter Relocation Charge	Actual
Damage to Meter Equipment	Actual



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