

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF CUMBERLAND )	CASE NO.
COUNTY WATER DISTRICT FOR A RATE )	2022-00291
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 October 14, 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 October 14, 2022 Order, Cumberland County Water District (Cumberland 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 Cumberland 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 FEB 14 2023

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 CUMBERLAND COUNTY WATER DISTRICT

Cumberland County Water District (Cumberland 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 2,857 residential customers, 47 commercial customers, 5 industrial customers, and 1 public authority that reside in Cumberland County, Kentucky.<sup>1</sup> On September 21, 2022, Cumberland District filed an application with the Commission requesting to adjust its water rates pursuant to 807 KAR 5:076. The application was filed pursuant to the Commission's Order in Case No. 2020-00188 to file an application by July 28, 2021.<sup>2</sup> On June 28, 2021, Cumberland District requested a six-month extension of time to file the application.<sup>3</sup> On July 15, 2021, the Commission deferred the motion and requested additional information.<sup>4</sup> On August 4,

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<sup>1</sup> *Annual Report of Cumberland County Water District to the Public Service Commission for the Calendar Year Ended December 31, 2021* (2021 Annual Report) at 12 and 49.

<sup>2</sup> Case No. 2020-00188, *Electronic Application of the Cumberland County Water District to Issue Securities in the Approximate Principal Amount of \$1,570,000 for the Purpose of Refunding Certain Outstanding Obligations of the District Pursuant to the Provisions of KRS 278.300 and 807 KAR 5:001*, (Ky. PSC July, 28, 2020).

<sup>3</sup> Case No. 2020-00188, Post Case Referenced Correspondence, Motion for Extension (filed July 28, 2021).

<sup>4</sup> Case No. 2020-00188, Order (Ky. PSC July 15, 2021).

2021, Cumberland District provided its response to the Commission's request for information.<sup>5</sup> The Commission denied the request on August 22, 2022 and ordered Cumberland District to file an application as soon as possible.<sup>6</sup> The Commission Staff notes that the Commission's January 30, 2023 Order in Case No. 2022-00244 incorporated the record of this proceeding into an ongoing investigation.<sup>7</sup> Further, Commission Staff notes that a hearing will be held February 23, 2023, in the investigation proceeding.

Cumberland District's last base rate increase pursuant to the alternative rate filing procedure was in Case No. 2002-00477.<sup>8</sup> Cumberland District has not sought a general adjustment in rates by any means, other than through financing approval under KRS 278.023, Approval of Federally funded Construction Projects and in conjunction with an application for a Certificate of Public Convenience and Necessity, since that time.

To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated October 14, 2022. Commission Staff issued its first request for information (Staff's First Request) on October 14, 2022. Cumberland District filed its response to Staff's First Request on November 3, 2022. Staff issued its second request for information (Staff's Second Request) on November 17, 2022, and Cumberland District filed its response on December 8, 2022. Commission Staff issued a Third Request

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<sup>5</sup> Case No. 2020-00188, Post Case Referenced Correspondence, Response to Request for Additional Information (filed Aug. 4, 2021).

<sup>6</sup> Case No. 2020-00188, Order (Ky. PSC Aug. 22, 2021).

<sup>7</sup> Case No. 2022-00244, *Electronic Alleged Failure Of Cumberland County Water District And Its Officers, Eric Carver, Garland Hieneman, Jay Cary, Mark Vibbert, Troy Norris, And Its Manager, Matthew Dyer, to Comply With a Commission Order, KRS 278.990* (Ky. PSC Jan. 30, 2023).

<sup>8</sup> Case No. 2002-00477, *Application of Cumberland County Water District for Approval of the Proposed Increase in Rates for Water Service* (Ky. PSC May 6, 2003).

for Information (Staff's Third Request) on January 5, 2023, and Cumberland District filed its responses on January 19, 2023.

### WATER LOSS

The Commission notes that in its 2021 Annual Report, Cumberland District reported a water loss of 35.2088 percent.<sup>9</sup> Commission regulation 807 KAR 5:066 Section (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 35.2088 percent water loss, the annual cost of water loss in excess of 15.00 percent is \$96,451 and the total annual cost of water loss to Cumberland District is \$168,042 as shown in the table below.

Total Water Loss	Purchased Water	Power	Total
Pro Forma Purchases	\$ 423,902	\$ 53,370	\$ 477,272
Water Loss Percent	35.2088%	35.2088%	35.2088%
Total Water Loss	<u>\$ 149,251</u>	<u>\$ 18,791</u>	<u>\$ 168,042</u>

Disallowed Water Loss	Purchased Water	Power	Total
Pro Forma Purchases	423,902	53,370	\$ 477,272
Water Loss in Excess of 15%	20.2088%	20.2088%	20.2088%
Disallowed Water Loss	<u>\$ 85,666</u>	<u>\$ 10,785</u>	<u>\$ 96,451</u>

### DISCUSSION

To comply with the requirements of 807 KAR 5:076, Section 9,<sup>10</sup> Cumberland District used the calendar year ended December 31, 2021, as the basis for its application. Cumberland District determined that a base rate revenue increase of \$260,122, or

<sup>9</sup> 2021 Annual Report at 57.

<sup>10</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.

18.21 percent, was necessary to achieve the revenue requirement as shown in the table below.<sup>11</sup>

Pro Forma Operating Expenses	\$ 1,418,155
Plus: Average Annual Principal and Interest Payments	287,805
Additional Working Capital	<u>57,561</u>
Overall Revenue Requirement	1,763,521
Less: Other Operating Revenue	(73,894)
Interest Income	<u>(1,386)</u>
Revenue Required from Rates	1,688,241
Less: Pro Forma Present Rate Service Revenues	<u>(1,428,119)</u>
Required Revenue Increase	<u>\$ 260,122</u>
Percentage Increase	<u>18.21%</u>

To determine the reasonableness of the rates requested by Cumberland District, Commission Staff performed a limited financial review of Cumberland 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>12</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.

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<sup>11</sup> Application, Revenue Requirements Using Debt Service Coverage Method at 23.

<sup>12</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, *Application of Hardin County Water 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 Water 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); Case No. 2017-00417, *Electronic Proposed Adjustment of the Wholesale Water Service Rates of Lebanon Water Works* (Ky. PSC July 12, 2018).

Commission Staff's findings are summarized in this report. Jeff Abshire and Noah Abner reviewed the calculation of Cumberland District's Overall Revenue Requirement and Eddie Beavers reviewed Cumberland District's reported revenues and rate design.

### SUMMARY OF FINDINGS

1. Overall Revenue Requirement and Required Revenue Increase. By applying the Debt Service Coverage (DSC) method, as generally accepted by the Commission, Commission Staff found that Cumberland District's required revenue from water sales is \$1,607,020 to meet the Overall Revenue Requirement of \$1,632,120 and that a \$178,901 revenue increase, or 12.53 percent, to pro forma present rate revenues is necessary to generate the Overall Revenue Requirement.

2. Monthly Water Service Rates. Cumberland District proposed to increase its monthly retail water service rates by approximately 18.21 percent.<sup>13</sup> Cumberland District has not performed a cost-of-service study (COSS). Cumberland District stated that it did not complete a COSS at this time as there have been no material changes in the water system.<sup>14</sup>

The Commission has previously found that the allocation of a revenue increase 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 and in the absence of a COSS. Finding no such evidence in this case, Commission Staff has followed the method previously accepted by the Commission and has allocated the

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<sup>13</sup> Application, Exhibit A, Reasons for Application.

<sup>14</sup> Cumberland District's Response to Commission Staff's First Request for Information (Staff's First Request) (filed Nov. 3, 2022), Item 15a and 15b.

\$178,901 revenue increase evenly across the board to Cumberland District's monthly retail water service rates.

The rates set forth in the Appendix to this report are based upon the revenue requirement, as calculated by Commission Staff, and will produce sufficient revenues from water sales to recover the \$1,607,020 Revenue Required from Rates, an approximate 12.53 percent increase. These rates, including a water loss recovery surcharge of \$2.85 as recommended by Commission Staff in section 4.0 of this report, will increase a typical residential customer's monthly water bill from \$37.25 to \$44.77, an increase of \$7.52, or approximately 20.18 percent.<sup>15</sup> The surcharge represents 7.65 percent of the increase.

3. Nonrecurring Charges. Following the Commission's recent decisions,<sup>16</sup> Commission Staff has reviewed Cumberland 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 most recent cost justification information provided in response to

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<sup>15</sup> The average residential customer uses 3,059 gallons per month. Application, Exhibit K, Compliance with 807 KAR 5:076, Section 5, Legal Notice Regarding the Cumberland County Water District at 386.

<sup>16</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).

Commission Staff's First Request.<sup>17</sup> Such adjustments result in the following revised nonrecurring charges:

Nonrecurring Charges	
After Hours Charge	\$50.00
Field Collection Charge	\$18.00
Meter Reread Charge	\$18.00
Meter Test Charge	\$18.00
New Service Charge	\$18.00
Re-Connection Charge	\$36.00
Returned Check Charge	\$3.50
Service Charge	\$18.00

Commission Staff followed Commission precedent and made the adjustments to the Nonrecurring Charges which results in a decrease to the charges and an increase to the total revenue requirement of \$7,680 as shown below.<sup>18</sup>

	Num	Current Rate	Total Collected	Revised Rate	Inc / (Dec)	Pro Forma
<i>Miscellaneous Service Revenues</i>						
After Hours Charge	2	\$50.00	\$100	\$50.00	\$0	\$100
Field Collection Charge	87	\$35.00	3,045	\$18.00	(1,479)	1,566
Meter Re-read Charge	0	\$35.00	0	\$18.00	0	0
Meter Test Charge	0	\$65.00	0	\$18.00	0	0
New Service Charge	254	\$35.00	8,890	\$18.00	(4,318)	4,572
Re-Connection Charge	43	\$70.00	3,010	\$36.00	(1,462)	1,548
Returned Check Charge	18	\$25.00	450	\$3.50	(387)	63
Service Charge	2	\$35.00	70	\$18.00	(34)	36
Total			<u>\$15,565</u>		<u>(\$7,680)</u>	<u>\$7,885</u>

<sup>17</sup> Commission Staff's First Request (filed Nov. 3, 2022), Item 14, 14\_Nonrecurring\_Charge\_Cost\_Justification.pdf.

<sup>18</sup> Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020).



4. Water Loss Reduction Surcharge. Upon its review of Cumberland District's Annual Reports on file with the Commission for the calendar years 2017 through 2021,<sup>19</sup> the Commission Staff notes that Cumberland District's reported water loss consistently exceeded the 15 percent limitation established in 807 KAR 5:066, Section (6) (3). The table below displays Cumberland District's reported water loss percentages, cost to purchase and pump water, cost of water loss in excess of the 15 percent limitation, and the total cost of water loss for the past five years. Purchased water cost in 2021 was adjusted for a pro forma cost adjustment.

Year	Reported Percentage Water Loss	Purchased Water and Power	Cost of Water Loss in Excess of 15%	Total Cost of Water Loss
2017	28.8870%	\$ 403,191	\$ 55,991	\$ 116,470
2018	34.6381%	462,112	90,750	160,067
2019	39.8999%	503,940	125,481	201,072
2020	40.6964%	534,818	137,429	217,652
2021	35.2088%	477,272	96,451	168,042

While Cumberland District did not request a surcharge in its application to fund its efforts to correct the chronic water loss, the use of a surcharge is consistent with prior Commission action in cases involving water utilities with excessive unaccounted for water loss.<sup>20</sup> The Commission has ordered surcharges even when a utility has not specifically

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<sup>19</sup> *Annual Reports of Cumberland County Water District for the Years Ended December 31, 2017 through 2021*, Water Utility Expense Accounts and Water Statistics pages.

<sup>20</sup> See Case No. 96-126, *An Investigation into the Operations and Management of South Hopkins 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); 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); and 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.

requested a surcharge,<sup>21</sup> and recently, the Commission has allowed water utilities with reported water loss above the 15 percent threshold to assess water loss reduction surcharges.<sup>22</sup>

Recognizing 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 to authorize Cumberland District to assess a monthly water loss reduction surcharge of \$2.85<sup>23</sup> per active meter for 48 months (total of \$386,460), with a review of the necessity to continue the surcharge before the 48-month period expires. Commission Staff also recommends that 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. In addition, Commission Staff recommends that Cumberland District be required 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

Cumberland District's Pro Forma Operating Statement for the test year ended December 31, 2021, as determined by Staff, appears below.

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<sup>21</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>22</sup> 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).

<sup>23</sup> \$96,451 (Cost of Water and Power in Excess of 15% Water Loss Limit) ÷ 2,825 average active meters ÷ 12 months = \$2.85 per month. Total surcharge for 48 months estimated at \$2.85 x 48 x 2,825 = \$386,460. Average active meters assumes six months with 2,910 meters and six months with 2,739 meters due to meters located near Dale Hollow Lake that are only active during a portion of the year.

	Test Year	Adjustment	(Ref)	Pro Forma
Operating Revenues				
Sales of Water	\$ 1,467,059	\$ (38,940)	(A)	\$ 1,428,119
Late Payment Penalties		15,829	(B)	15,829
Miscellaneous Service Revenues		24,953	(C)	
		(17,068)	(C)	7,885
Other Water Revenues		33,112	(D)	
		(33,112)	(D)	0
<b>Total Operating Revenues</b>	<b>1,467,059</b>	<b>(15,226)</b>		<b>1,451,833</b>
Operating Expenses				
Operation and Maintenance Expenses				
Salaries and Wages - Employees	311,763	39,738	(E)	
		(14,865)	(F)	336,636
Salaries and Wages - Commissioners	8,850	0	(G)	8,850
Employee Pensions and Benefits	51,803	14,157	(H)	65,960
Purchased Water	403,015	20,887	(I)	
		(85,666)	(J)	338,236
Purchased Power for Pumping	53,370	(10,785)	(J)	42,585
Materials and Supplies	121,822	(44,593)	(F)	77,229
Contractual Services	26,961			26,961
Transportation Expense	52,106			52,106
Insurance	21,389			21,389
Regulatory Commission Expense	53,982	(51,174)	(K)	2,808
Miscellaneous Expense	11,239	51,174	(K)	62,413
<b>Total Operation and Maintenance Expenses</b>	<b>1,116,300</b>	<b>(81,127)</b>		<b>1,035,173</b>
Taxes Other Than Income - FICA	28,401			28,401
Depreciation	325,017	(106,631)	(L)	
		4,794	(M)	223,180
<b>Total Operating Expenses</b>	<b>1,469,718</b>	<b>(182,964)</b>		<b>1,286,754</b>
Net Operating Income	(2,659)	167,738		165,079
Interest Income	1,386			1,386
<b>Income Available to Service Debt</b>	<b>\$ (1,273)</b>	<b>\$ 167,738</b>		<b>\$ 166,465</b>

(A) Billing Analysis Adjustment. Cumberland District proposed to decrease its test-year revenues from retail water sales of \$1,467,059 by \$38,940 to reflect the Billing Analysis.<sup>24</sup> Commission Staff has reviewed the Billing Analysis and the responses to three data requests and agree with Cumberland District's adjustment.

<sup>24</sup> 2021 Annual Report at 49.

(B) Forfeited Discounts. Cumberland District stated in its application that it had misclassified its Forfeited Discounts as General Water Sales. Cumberland District proposed an adjustment of \$15,829 to reflect the reclassification of the amount for its test year Forfeited Discounts. Commission Staff agrees that the Forfeited Discounts have been misclassified and should be reclassified as proposed by Cumberland District.

(C) Miscellaneous Service Revenues. Cumberland District reported test year Miscellaneous Service Revenues of \$24,953. Cumberland District stated that some of the components would recur but did not specify the items. Commission Staff reviewed the individual line items in Cumberland District's general ledger and reduced Miscellaneous Service Revenues by \$17,068 based on Commission Staff's assessment of non-recurring items.<sup>25</sup>

(D) Other Water Revenues. Cumberland District reported test year Other Water Revenues of \$33,112 that were misclassified as General Water Sales.<sup>26</sup> Cumberland District received Compensation in Aid of Construction Funds of \$24,240 and Miscellaneous Revenues of \$8,872. These amounts were inappropriately reported as Other Water Revenues and should be removed.<sup>27</sup> Cumberland District stated that these items are not expected to recur, and Commission Staff removed the amounts from the Pro Forma.

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<sup>25</sup> Cumberland District's Response to Staff's Third Request (filed Jan. 19, 2023), Item 4; Cumberland District's Response to Staff's First Request (filed Nov. 3, 2022), Exhibit A.1.a 2021\_General\_Ledger.xlsx.

<sup>26</sup> Application, Item 4, 4\_SAO\_w\_attachments.pdf

<sup>27</sup> Cumberland District's Response to Staff's Third Request (filed Jan. 19, 2023), Item 4.

(E) Salaries and Wages - Employees. In its application, Cumberland District proposed an increase of \$39,738 to Salaries and Wages – Employees expense to reflect the net effect of vacancies, new hires, and authorized wage increases after the test year.<sup>28</sup> Commission Staff reviewed Cumberland District’s calculations and determined the proposed adjustments are an accurate representation of the increase in the annual labor expense to Cumberland District. Accordingly, Commission Staff increased Salaries and Wages Employees \$39,738.

(F) Capitalization of Cost of Customer Taps. During the test year, Cumberland District installed seventy-eight meter connections; none of which were capitalized. Cumberland District stated, “It appears that no cost associated with these taps is represented in the Depreciation Schedule”.<sup>29</sup> Commission Staff recommends the Commission require, in its final Order in this proceeding, that Cumberland District establish a process to facilitate capitalization of customer tap costs by its accounting personnel. Commission Staff calculated the cost of the installed taps and reduced Salaries and Wages expense and Materials and Supplies expense by \$14,865 and \$44,593, respectively, as shown in the calculations below.

Tap Fees	\$	59,458
Labor Percentage		25%
Reduction to Labor Expense	<u>\$</u>	<u>14,865</u>
Reduction to Materials and Supplies Expense	<u>\$</u>	<u>44,593</u>

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<sup>28</sup> Application, Exhibit C, Statement of Adjusted Operations, References, Adjustment E.

<sup>29</sup> Cumberland District’s Response to Commission Staff’s Second Request for Information (Staff’s Second Request) (filed Dec. 8, 2022), Item A.3.c at 11.

In addition to the reduction in expense, Commission Staff capitalized the \$44,593 amount in its adjustments to Depreciation Expense described in item (M) below.

(G) Salaries and Wages – Commissioners. In the test year, Cumberland District reported \$8,850 for Salaries and Wages – Officer Expense. Cumberland District did not propose an adjustment to Commissioner compensation. Commission Staff reviewed Commissioner compensation information provided by Cumberland District and determined that the highest full year compensation during 2021 for any Commissioner was \$3,025.<sup>30</sup>

Cumberland District pays commissioners on a per occurrence (meeting, check signing) basis but was not able to provide documentation that authorized the payment structure or the amounts.<sup>31</sup> Cumberland District stated,

[N]either the District or the Cumberland County Fiscal Court has been able to locate any document authorizing the current compensation. The current compensation amount is \$75.00 per board meeting and \$25.00 per occurrence when board members are required to appear for other District business. It is thought that these compensation amounts have been in place since at least 2007.<sup>32</sup>

KRS 74.020(6) states that “[e]ach commissioner shall receive an annual salary of not more than thirty-six hundred dollars (\$3,600)...” and that

[A]ny such amount the salary shall be fixed by the county judges/executive with the approval of the fiscal court; in multicounty districts, it shall be fixed by the agreement between the county judges/executive with the approval of their fiscal courts. In fixing and approving the salary of the commissioners, the county judge/executive and the fiscal

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<sup>30</sup> Cumberland District’s Response to Staff’s First Request (filed Nov. 3, 2022), Exhibit A.5.a, Commissioner Compensation.xlsx.

<sup>31</sup> Cumberland District’s Response to Staff’ First Request (filed Nov. 3, 2022), Item A.5.

<sup>32</sup> Cumberland District’s Response to Staff’s First Request (filed Nov. 3, 2022), Item A.5.

court shall take into consideration the financial condition of the district and its ability to meet its obligations as they mature.

Commission Staff recommends that Cumberland District request the Cumberland County Fiscal Court to update its authorization of Cumberland District Commissioner compensation amounts as soon as possible. Commission Staff further recommends that Cumberland District request the Cumberland County Fiscal Court to include Cumberland District Commissioner compensation authorization in Fiscal Court minutes upon the appointment or reappointment of each future Cumberland District commissioner. Commission Staff notes the required fixed salary is to be set by the fiscal court. Paying Commissioners per meeting or occurrence creates the possibility that a commissioner could be paid more than the statutorily allowable amount in the event the utility must hold more meetings than expected, or the commissioners have more frequent occurrences where they are needed to attend to utility business. Commission Staff accepts the proposed amount of \$8,850 without further adjustment. However, Commission Staff recommends that Cumberland District seek to have the salaries of its board of commissioners formally approved by the Cumberland County Fiscal Court and that such approval be reflected in the minutes of that body and kept in Cumberland District's official records.

(H) Benefits – Employees. In its application, Cumberland District proposed a net increase of \$934 in Employee Pensions and Benefits costs to reflect the current number of employees and the current employer sponsored share of health and life insurance. Commission Staff notes that Cumberland District provided costs for uniforms and an annual employee bonus in its benefits calculations, but these items are not

classified as benefits in the general ledger nor are they considered benefits.<sup>33</sup> Cumberland District requires its employees to contribute 20 percent of the cost of their health insurance coverage.<sup>34</sup> In its Order of June 20, 2019, in Case No. 2019-00053,<sup>35</sup> the Commission found that as long as the employee contribution rate for health insurance is at least 12 percent, it will not make a further adjustment to the national average. Cumberland District submitted a \$1,503 adjustment, which is a component of its proposed increase of \$934, to reduce employee health insurance expense for ratemaking purposes to align the expense with the national average employer contribution rate. Commission Staff does not consider the additional adjustment as necessary in view of Cumberland District's 20 percent withholding requirement and did not include the \$1,503 reduction in its calculations. Commission Staff reviewed Cumberland District's calculations and determined that benefits cost should be increased by an additional \$14,157 as shown below:

<b>Description</b>	<b>Test Year</b>	<b>Adjustments</b>	<b>Pro Forma</b>
Medical Premiums	\$ 57,931	\$ 17,210	\$ 75,141
Employee Contributions ( )	(11,585)	(3,443)	(15,028)
Life Insurance	976	(200)	776
Anthem Supplemental	3,433	0	3,433
Other Net	1,048	590	1,638
<b>Total</b>	<b>\$ 51,803</b>	<b>\$ 14,157</b>	<b>\$ 65,960</b>

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<sup>33</sup> Application, Exhibit C, Statement of Adjusted Operations, References, Adjustment F.

<sup>34</sup> Cumberland District's Response to Staff's First Request (filed Nov. 3, 2022), Item A.1.d, Exhibit A3 Employee Benefit Information.

<sup>35</sup> Case No. 2019-00053, *Electronic Application of Jackson Purchase Energy Corporation for a General Adjustment in Existing Rates* (Ky. PSC June 20, 2019) at 9.



In its review of the general ledger,<sup>36</sup> Commission Staff identified benefit payments to Anthem Blue Cross Blue Shield (Anthem) and AFLAC that were not disclosed in Cumberland District's benefits description. Cumberland District stated that the payments to Anthem were inadvertently overlooked and should have been reported. Cumberland District further stated that the AFLAC payments are for supplemental coverage that employees may purchase at cost through the District, and thus, are not considered a benefit.<sup>37</sup> Commission Staff determined that the omitted Anthem payments were not material in aggregate and carried forward the test year payments for Pro Forma purposes.

The minutes of Cumberland District's May 9, 2022 Board of Commissioners' meeting state "Discussed Health Insurance for Board Members."<sup>38</sup> The minutes do not indicate if any action was taken. Cumberland District provided a copy of an invoice for employee medical insurance that included coverage for one commissioner. The commissioner's name was highlighted with a comment by Cumberland District that stated, "Cost of board member coverage is paid by CCWD, but then reimbursed to CCWD by board member".<sup>39</sup> Cumberland District subsequently stated that only one commissioner has received coverage, which began July 1, 2022, and that the commissioner's reimbursements were posted for July coverage on August 24, 2022, for \$155.30 and for

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<sup>36</sup> Cumberland District's Response to Staff's First Request (filed Nov. 3, 2022), Exhibit A.1.a 2021 General Ledger.xlsx.

<sup>37</sup> Cumberland District's Response to Staff's Second Request (filed Dec. 8, 2022), Item A.4.c.

<sup>38</sup> Cumberland District's Response to Staff's First Request (filed Nov. 3, 2022), Exhibit A4 2022 Board Meeting Minutes.

<sup>39</sup> Cumberland District's Response to Staff's First Request (filed Nov. 3, 2022), Item A.1.e – Current Benefit Invoice.

August coverage on November 2, 2022, for \$403.78.<sup>40</sup> The table below shows the difference between Cumberland District’s stated board member reimbursement amount and the actual cost of the insurance. Commission Staff notes that the payment amounts noted above represent approximately 19 percent of the cost of the insurance, which is in contradiction to Cumberland District’s statement above that the cost is reimbursed by the board member.

	Cost Per Week	Weeks in Year	Year	Monthly
Cumberland Response 12-08-22 (4d)	\$ 31.06	52	\$1,615.12	\$ 134.59
KLC Invoice Nov 2022	163.58	52	8,506.20	708.85
Difference	<u>\$ 132.52</u>		<u>\$6,891.08</u>	<u>\$ 574.26</u>
Commissioner Contribution to Cost	<u>19.0%</u>		<u>19.0%</u>	<u>19.0%</u>

Additionally, in Case No. 2019-00268 <sup>41</sup> the Commission found that:

Since water district commissioners are vested with all relevant powers to manage and oversee water districts,<sup>42</sup> except for the power to fix their salary authorized by KRS 74.020(6), which is assigned to the county judge executive and fiscal court,<sup>43</sup> a water district would be unable to provide its commissioners health insurance and other similar benefits

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<sup>40</sup> Cumberland District’s Response to Staff’s Second Request (filed Dec. 8, 2022), Item 4.d.

<sup>41</sup> Case No. 2019-00268, *Application of Knott County Water and Sewer District for an Alternative Rate Adjustment* (Ky. PSC Jan. 31, 2020).

<sup>42</sup> KRS 74.020(1) (“A water district shall be administered by a board of commissioners which shall control and manage the affairs of the district.”); KRS 74.070 (“All corporate powers of the water district shall be exercised by, or under the authority of, its commission.”) See also KRS 65A.080(1) (requiring the governing body of each “special purpose government entity” to adopt a budget and prohibiting any “special purpose government entity” from expending funds in a manner inconsistent with their budget and any amendment thereto.).

<sup>43</sup> KRS 74.020(6).

without an official action by the water district commissioners.<sup>44</sup> Thus, by prohibiting water district commissions from participating in official actions that directly benefit themselves financially, the General Assembly effectively prohibited water districts from receiving additional benefits to compensate them for their work on the board, which further indicates the General Assembly's intent to limit the total compensation of water district commissions to amounts specifically authorized by statute. The Commission finds that the General Assembly intended to limit the water districts' total compensation to commissioners for their service on a water district's board to amounts specifically authorized by KRS Chapter 74. Therefore, the Commission finds that Knott District may not offer benefits to the Commissioners on the Knott District Board of Commissioners pursuant to KRS Chapter 74 and should cease doing so immediately.

As noted in KRS 74.020(6) and as stated above by the Commission, a commissioner's benefits are limited to what is specifically authorized by the General Assembly. Commission Staff cannot confirm that this benefit was approved by either the Cumberland District Board of Commissioners or the Cumberland County Fiscal Court. Commission Staff recommends that the Commission explore this issue in Case No. 2022-00244. Further, Commission Staff recommends that Cumberland District voluntarily cease this practice. This recommendation is made because neither the amount of commissioner compensation nor the process of Cumberland District paying for health insurance for its commissioners is supported and documented in the minutes of Cumberland District's Board meetings or from the Fiscal Court.

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<sup>44</sup> KRS 74.020(6) presumably gives the county judge executive and fiscal court the authority to fix the salary of the water district commissioners to avoid just this issue. Further, while KRS 74.050 authorizes the water district board to establish the additional compensation, if any, to be paid to the treasurer of the board, the treasurer could avoid violating the prohibition against taking official actions that benefit him financially by properly recusing himself from such an action. Conversely, there would be no viable way for water district commissioners to provide themselves insurance benefits without involving themselves in the decision to do so.

(I) Purchased Water. Cumberland District purchases water from the cities of Burkesville and Albany. Cumberland District did not propose an adjustment to purchased water cost. Commission Staff discovered in its review of the general ledger and purchase quantities provided by Cumberland District<sup>45</sup> that total purchased water expense for the test period was understated by \$20,887. Commission Staff adjusted purchased water cost for this amount to reflect a total cost of \$423,902 for 2021.

	Burkesville	Albany	Total
Gallons	166,170.65	31,731.00	197,902
Current Purchase Rate	\$ 2.150	\$ 2.100	\$ 2.1420
Pro Forma Cost	<u>\$ 357,267</u>	<u>\$ 66,635</u>	<u>\$ 423,902</u>
Test Year General Ledger			403,015
Pro Forma Adjustment			<u><u>\$ 20,887</u></u>

(J) Water Loss. In its application, Cumberland District proposed adjustments to decrease Purchased Water Expense by \$81,449 to account for the district's water loss in excess of 15 percent.<sup>46</sup> In addition, Cumberland District proposed a decrease to Purchased Power expense of \$10,785 to reflect the disallowance of Purchase Power Expense attributable to water loss above 15 percent.<sup>47</sup> The average cost of purchased water using the corrected amounts is \$2.142 per thousand gallons.<sup>48</sup> Using the corrected average, the total disallowed purchased water attributed to water loss should be \$85,666 as shown below. Commission Staff agrees that Cumberland District's proposed

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<sup>45</sup> Application, Exhibit A 1.a, 2021 General Ledger; Cumberland District's Response to Staff's First Request (filed Nov. 3, 2022), Exhibit A.9, Purchased Water Information.

<sup>46</sup> Application, Exhibit C, Statement of Adjusted Operations, References, Adjustment G.

<sup>47</sup> Application, Exhibit C, Statement of Adjusted Operations, References, Adjustment G.

<sup>48</sup> Test Year Purchased Water Expense \$423,902 / 197.902 million Gallons Purchased in Test Period = Average Cost per 1,000 gallons \$2.142.

adjustment to Purchased Power is reasonable in all material respects and decreased Purchased Power expense \$10,785.

Disallowed Water Loss	Purchased Water	Power	Total
Pro Forma Purchases	423,902	53,370	\$ 477,272
Water Loss in Excess of 15%	20.2088%	20.2088%	20.2088%
Disallowed Water Loss	\$ 85,666	\$ 10,785	\$ 96,451

(K) Regulatory Commission Expense. In its application, Cumberland District reported test year Regulatory Commission Expense of \$53,982. The components of Cumberland District's reported amount are shown in the table below. Commission Staff reviewed Cumberland District's general ledger and concluded that \$2,808, which represents its liability for the annual PSC assessment, is applicable to Regulatory Commission Expense. Based on its review, Commission Staff concluded that the remaining \$51,174 should be reclassified to Miscellaneous Expense as shown in the table below.<sup>49</sup>

Description	Amount
Administrative Expense	\$ 60,074.92
Administrative Expense:Uniform & Outerwear	2,917.19
Administrative Expense:6750-00 · Office Expense	(20,659.81)
Administrative Expense:6750-00 · Office Expense:6750-10 · Postage	11,650.20
Classified by Cumberland District as Regulatory Commission Expense	\$ 53,982.50
Commission Staff Classified as Regulatory Commission Expense	(2,808.32)
Amount Reclassified to Miscellaneous Expense by Commission Staff	\$ 51,174.18

(L) Depreciation Expense. In its application, Cumberland District reported test year Depreciation Expense of \$325,017.<sup>50</sup> To evaluate the reasonableness of the

<sup>49</sup> Application, Exhibit C, Schedule of Adjusted Operations.

<sup>50</sup> Application, Exhibit C, Schedule of Adjusted Operations.

depreciation practices of small water utilities, the Commission has historically relied upon the report published in 1979 by the National Association of Regulatory Utility Commissioners (NARUC) titled *Depreciation Practices for Small Water Utilities* (NARUC Study). 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. Commission Staff identified assets classified as Transmission and Distribution with a net book value of \$7,255,540.09 that were being depreciated at an average life of 37.85 years. Commission Staff recalculated depreciation for these assets based on an average life of 62.5 years which resulted in a reduction of depreciation expense by \$106,631.

Asset Group	Asset #	Date in Service	Cost	Applicant Life	Current Depreciation	Commission Staff Life	Calculated Full Year Depreciation	Reduction
Transmission and Dist Eqpt	Group		11,014,591		270,357	62.50		
Less Zero Net Book Value Item	124		(253,350)					
Less Zero Net Book Value Item	125		(520,261)					
Less Zero Net Book Value Item	128		(5,861)					
Less Zero Net Book Value Item	130		(2,260)					
Undepreciated Group			<u>10,232,859</u>	<u>37.85</u>	<u>270,357</u>	<u>62.50</u>	<u>163,726</u>	<u>(106,631)</u>

(M) Depreciation – Adjustment for Full Year Depreciation and Capitalized Asset Adjustments. Commission Staff identified three assets that were capitalized during 2021 and depreciated for a fractional year but Cumberland District did not propose a Pro Forma adjustment to reflect full year depreciation. Additionally, Commission Staff calculated depreciation expense on capitalized tap fees. Depreciation expense was increased by \$4,794 for these adjustments.

Asset Group	Asset #	Date in Service	Cost	Applicant Life	Current Depreciation	Commission Staff Life	Full Year Depreciation	Adjustment
Meter / Meter Installation	221	10/21/21	36,624	40	152.60	40	915.60	\$ 763
Meter / Meter Installation	222	01/25/21	24,236	40	555.41	40	605.90	50
Transportation	220	02/12/21	2,000	10	183	10	200.00	17
Capitalize Tap Fees - Labor			14,865		0	15	991.00	991
Capitalize Tap Fees - Materials			44,594		0	15	2,972.93	2,973
Total							<u>\$ 4,794</u>	

OVERALL REVENUE REQUIREMENT AND  
REQUIRED REVENUE INCREASE

The Commission has historically applied a Debt Service Coverage (DSC) method to calculate the Overall Revenue Requirement of water districts and water associations. This method allows for recovery of (1) cash-related pro forma operating expenses; (2) recovery of depreciation expense, a non-cash item, to provide working capital;<sup>51</sup> (3) the average annual principal and interest payments on all long-term debts; and (4) working capital that is in addition to depreciation expense.

	Cumberland District	Commission Staff	
Pro Forma Operating Expenses	\$ 1,418,155	\$ 1,286,754	
Plus: Average Annual Principal and Interest Payments	287,805	287,805	(1)
Additional Working Capital	57,561	57,561	(2)
Overall Revenue Requirement	1,763,521	1,632,120	
Less: Other Operating Revenue	(73,894)	(23,714)	
Interest Income	(1,386)	(1,386)	
Revenue Required from Rates	1,688,241	1,607,020	
Less: Pro Forma Present Rate Service Revenues	(1,428,119)	(1,428,119)	
Required Revenue Increase	\$ 260,122	\$ 178,901	
Percentage Increase	18.21%	12.53%	

1. Average Annual Principal and Interest Payments. At the time of Commission Staff’s review, Cumberland District had four outstanding loans from the

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<sup>51</sup> The Kentucky Supreme Court has held that the Commission must permit a water district to recover its depreciation expense through its rates for service to provide internal funds for renewing and replacing assets. See *Public Serv. Comm’n of Kentucky v. Dewitt Water Dist.*, 720 S.W.2d 725, 728 (Ky. 1986). Although a water district’s lenders require that a small portion of the depreciation funds be deposited annually into a debt reserve/depreciation fund until the account’s balance accumulates to a required threshold, neither the Commission nor the Court requires that revenues collected for depreciation be accounted for separately from the water district’s general funds or that depreciation funds be used only for asset renewal and replacement. The Commission has recognized that the working capital provided through recovery of depreciation expense may be used for purposes other than renewal and replacement of assets. See Case No. 2012-00309, *Application of Southern Water and Sewer District for an Adjustment in Rates Pursuant to the Alternative Rate Filing Procedure for Small Utilities* (Ky. PSC Dec. 21, 2012).

United States Department of Agriculture Rural Development (RD), two outstanding loans from the Kentucky Rural Water Finance Corporation (KRWA), one loan from the Kentucky Infrastructure Authority, and one loan from Ditch Witch Financial Services.<sup>52</sup> Cumberland District requested recovery of the average annual principal and interest on its indebtedness based on a five-year average of the annual principal, and interest and fee payments for the years 2022 through 2026.<sup>53</sup> Commission Staff agrees with the methodology Cumberland District proposed and included \$287,805 in the calculation of the revenue requirement.

Possible Violation of KRS 278.300. Commission Staff is concerned that a 48-month lease / purchase contract that was executed with Ditch Witch Financial Services, effective July 15, 2020, does not conform with the requirements of KRS 278.300. Payments of \$1,118.59 will total \$53,692.32 at the end of the lease.<sup>54</sup> Cumberland District stated that to the best of its knowledge the debt was not authorized by the Commission.<sup>55</sup> Commission Staff recommends investigating this transaction further, either in the ongoing investigation in Case No. 2022-00244 or in an additional investigation.

2. Additional Working Capital. The DSC method, as historically applied by the Commission, includes an allowance for additional working capital that is equal to the minimum net revenues required by a district's lenders that are above its average annual debt payments. Cumberland District requested recovery of an allowance for working

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<sup>52</sup> Case 2016-00255, *Application of Cumberland County Water District for a Certificate of Public Convenience and Necessity and to Incur Indebtedness of \$100,000 for the Purchase of Metering System* (Ky. PSC Mar. 9, 2017).

<sup>53</sup> Application, Revenue Requirements Using Debt Service Coverage Method at 23.

<sup>54</sup> Application, Exhibit G.4, Lease Agreement at 179.

<sup>55</sup> Cumberland District's Response to Staff's First Request (filed Nov. 3, 2022), Item 11 at 28.



capital that is equal to 120 percent of its average annual debt payments for its long-term debt at the time of its application.<sup>56</sup> RD requires that Cumberland District charge rates that produce net revenues that are at least 120 percent of its average annual debt payments. Following the Commission's historic practice of including additional working capital, \$57,561 is included in the revenue requirement.

#### SUPPLEMENTAL COMMISSION STAFF COMMENTS

Commission Staff is concerned about the negative effects of Cumberland District not having a qualified accountant/financial manager on its staff or under contract to provide needed services. During its review of the general ledger for the test year, Commission Staff experienced considerable difficulty tracing transactions to determine their purpose and appropriateness for inclusion in the Pro Forma calculations. Commission Staff identified 190 accounting entries that were designated as audit adjustments in the test year.<sup>57</sup> Cumberland District stated that the General Manager is responsible for coding receipts and disbursements to the general ledger and that "annual reviews are performed by Cumberland District's auditor".<sup>58</sup> These statements beg the question of how Cumberland District commissioners can have meaningful discussions concerning the District's current financial operations and future capital needs in the absence of accurate financial information.

Commission Staff's concern is confirmed by Cumberland District's independent auditor's significant deficiency finding #2021-3 of its audited financial statements for the

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<sup>56</sup> Application, Revenue Requirements Using Debt Service Coverage Method at 23.

<sup>57</sup> Cumberland District's Response to Staff's First Request (filed Nov. 3, 2022), Exhibit A.1.a 2021 General Ledger.xlsx.

<sup>58</sup> Cumberland District's Response to Staff's Third Request (filed Jan. 19, 2023), Item A2.b.

year ended December 31, 2021. This is a repeat finding from prior audits. The finding states, “Due to limited internal resources, the District’s general ledger accounts are not being reviewed and adjusted to supporting detail on a regular monthly basis to ensure that all transactions are being recorded and account balances are accurate.” The auditor further noted the effect of this shortcoming by stating “[t]his condition prevents management and the Board from having accurate, reliable financial information on an ongoing basis in order to make informed decisions about the financial affairs of the District.”<sup>59</sup> Commission Staff recommends the Commission encourage Cumberland District to look beyond the cost of a staff position and either employ a qualified accountant, or enter into a contract for the services of a qualified accountant to perform accounting transaction coding and reporting functions to improve the quality of its interim financial information and facilitate the general manager’s time being better utilized on the operational and strategic needs of the District.

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<sup>59</sup> *Audited Financial Statements of Cumberland County Water District for the Years Ended December 31, 2013 through 2021.* (filed annually with Ky. PSC).

## Signatures

/s/ Jeff Abshire

Prepared by: Jeff Abshire  
Revenue Requirement Branch  
Division of Financial Analysis

/s/ Noah Abner

Prepared by: Noah Abner  
Revenue Requirement Branch  
Division of Financial Analysis

/s/ Eddie Beavers

Prepared by: Eddie Beavers  
Rate Design Branch  
Division of Financial Analysis

APPENDIX

APPENDIX TO COMMISSION STAFF'S REPORT OF THE KENTUCKY  
PUBLIC SERVICE COMMISSION IN CASE NO. 2022-00291 DATED FEB 14 2023

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

5/8- x 3/4-Inch Meter

First	2,000 Gallons	\$	32.75 Minimum Bill
Next	3,000 Gallons		0.00866 Per Gallon
Next	5,000 Gallons		0.00755 Per Gallon
Over	10,000 Gallons		0.00641 Per Gallon

1-Inch Meter

First	5,000 Gallons	\$	59.08 Minimum Bill
Next	5,000 Gallons		0.00755 Per Gallon
Over	10,000 Gallons		0.00641 Per Gallon

1 1/2-Inch Meter

First	12,500 Gallons	\$	112.47 Minimum Bill
Over	12,500 Gallons		0.00641 Per Gallon

2-Inch Meter

First	25,000 Gallons	\$	192.65 Minimum Bill
Over	25,000 Gallons		0.00641 Per Gallon

Dale Hollow State Park

First	300,000 Gallons	\$	1,956.56 Minimum Bill
Over	300,000 Gallons		0.00641 Per Gallon

Water Loss Reduction Surcharge

To be collected for 48 months or until a total amount of \$386,460 is collected for water loss reduction.	\$	2.85 Per Active Meter
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Nonrecurring Charges

After Hours Charge	\$50.00
Field Collection Charge	\$18.00
Meter Reread Charge	\$18.00
Meter Test Charge	\$18.00
New Service Charge	\$18.00
Re-Connection Charge	\$36.00
Returned Check Charge	\$3.50
Service Charge	\$18.00

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