

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF JOANN ESTATES UTILITIES, )	CASE NO. 2013-00307
INC. FOR RATE ADJUSTMENT FOR SMALL )	
UTILITIES PURSUANT TO 807 KAR 5:076 )	

ORDER

On August 5, 2013, Joann Estates Utilities, Inc. ("Joann Estates") tendered an application with the Commission pursuant to 807 KAR 5:076 requesting to increase its monthly flat sewer service rate from \$19.66 to \$35.00, an increase of \$15.34, or 78.03 percent. After Joann Estates filed additional documentation, the Commission accepted Joann Estates' application for filing on August 22, 2013. On December 3, 2013, the Commission issued an Order granting Destiny Hammond's motion to intervene.

By this Order, the Commission approves a flat monthly rate of \$34.71, an increase of \$15.05, or 76.55 percent, to Joann Estates' current rate.

Pursuant to the Commission's Order dated October 8, 2013, Commission Staff ("Staff") submitted a report finding that Joann Estates' adjusted test-year operations support a flat monthly rate of \$30.66<sup>1</sup> without inclusion of the \$9,600 for annual sludge-hauling expenses requested by Joann Estates in its Application. Staff found that inclusion of the sludge-hauling expense would increase the monthly rate by \$4.05<sup>2</sup> to \$34.71.

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<sup>1</sup> Staff Report at 2.

<sup>2</sup> *Id.* at 9.

Joann Estates filed responses to Staff's report on December 16, 2013, and January 8, 2014, providing additional evidence to support the sludge-hauling expense. It requested that the case stand submitted to the Commission for a decision without an informal conference or a formal hearing. On December 19, 2013, the Commission issued an Order stating that a formal hearing would not be held and that the record would be closed 21 days from the date of the Order, and that the matter was submitted for a decision.

On February 12, 2014, Joann Estates notified the Commission of its intent to place the proposed rates into effect for service rendered on and after February 22, 2014.<sup>3</sup> In response, the Commission directed Joann Estates to maintain appropriate records of its billing to permit any necessary refunds.

By Order issued February 24, 2014, the record was reopened to take additional information regarding sludge-hauling expenses. An informal conference was held on March 4, 2014, to discuss Joann Estates' sludge-hauling requirements. Notice of the informal conference was mailed to Ms. Hammond, but she did not contact the Commission and did not participate in the informal conference.

Having considered the evidence of record and being otherwise sufficiently advised, the Commission finds that:

1. Joann Estates, a Kentucky corporation, owns and operates sewage treatment and collection facilities that serve approximately 277 residential customers in

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<sup>3</sup> No action was necessary to suspend the effective date of Joann Estate's proposed rates for sewer service. Pursuant to 807 KAR 5:076, Section 7(1), an applicant who applies for a rate adjustment pursuant to the procedures set forth in 807 KAR 5:076 may not place its proposed rates into effect until the Commission approves those rates or six months from the date of the filing of its application.

Joann Estates, Timberland, and Wilmington Chiles Subdivisions in McCracken County, Kentucky.<sup>4</sup>

2. The calendar year ended December 31, 2012, should be used as the test year to determine the reasonableness of Joann Estates' existing and proposed rates.

3. Joann Estates has operated for over 30 years using five lagoons as sludge collection and retention basins. Operation of the lagoons has allowed Joann Estates to avoid sludge-hauling expenses in previous years, including the test year.<sup>5</sup>

4. In its Application, Joann Estates stated that one of its lagoons is inactive and that this lagoon has been used in previous years as a dumping area for sludge that was removed from the other four lagoons. It stated that a substantial amount of sludge has accumulated in the inactive lagoon that should now be hauled offsite. It stated that \$9,600 is the minimum annual expense required to remove sludge from this lagoon and requested to increase test-year expenses by this amount. In support of its request, Joann Estates provided a bid from Summit Contracting, LLC ("Summit") in the amount of \$365,250 that Joann Estates stated was to "fully remove the sludge which has accumulated in the inactive lagoon over the years."<sup>6</sup>

5. In its report, Staff found that rate recovery of the requested sludge removal costs was not appropriate in this proceeding without an analysis demonstrating that significant sludge removal from the lagoon was required; however, Staff agreed that

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<sup>4</sup> Staff Report at 1.

<sup>5</sup> *Id.* at 6.

<sup>6</sup> Application, Exhibit 2, Page 3, Explanation to Reference Item D.

recovery of \$9,600 annually for sludge removal costs may be appropriate if Joann Estates agreed to certain conditions.<sup>7</sup>

6. Joann Estates agreed to the conditions stated in the Staff's report.<sup>8</sup>

7. At the informal conference held on March 4, 2014, Joann Estates clarified the need for the requested \$9,600 annual sludge-hauling expense. It stated that recovery of this level of expense was necessary primarily to remove sludge from inside its five treatment plants, not from the inactive lagoon. It stated that any portion of the \$9,600 remaining after all necessary sludge hauling from inside the plants was complete would be expended to remove sludge from the inactive lagoon. Joann Estates reaffirmed its consent to Staff's conditions and further agreed to report the amounts expended for sludge hauled from inside the plants separately from the amounts expended for removal of sludge from the inactive lagoon.

8. It is necessary to remove excess sludge from a plant's aeration basins, clarifiers, and digesters for proper operations. By agreeing to the conditions established by Staff, Joann Estates has committed to expending \$9,600 annually for sludge removal. Rate recovery of this amount is appropriate in this proceeding.

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<sup>7</sup> Staff Report at 7-8.

<sup>8</sup> Letter dated Dec. 11, 2013, from B. G. Waid, President, Joann Estates Utilities, Inc. to Executive Director, Public Service Commission (filed Dec. 16, 2013).

9. Given that no basis exists to determine an appropriate rate of return for Joann Estates, use of an operating ratio<sup>9</sup> is appropriate to determine its allowable Net Operating Income (“NOI”).<sup>10</sup>

10. The Commission’s historic method of applying an operating ratio provides Joann Estates with an allowable NOI of \$13,459.<sup>11</sup>

11. As shown in Joann Estates’ adjusted operating statement that is set forth in Appendix A to this Order, operating revenues of \$115,370 are required to produce the allowable NOI.

12. After accounting for income taxes, the operating ratio resulting from the required revenue is 88.33 percent.<sup>12</sup>

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<sup>9</sup> Operating Ratio is defined as the ratio of expenses, including depreciation and taxes, to gross revenues. It is illustrated by the following equation:

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

<sup>10</sup> See, e.g., Case No 8468, *An Adjustment of the Rates of Plantation Hill Sewage Treatment Plant, Inc.* (Ky. PSC Jun. 25, 1982); 1 A.J G. Priest, *Principles of Public Utility Regulation* (Michie 1969) 220-224.

<sup>11</sup>

Pro Forma Operating Expenses Before Income Taxes	\$ 98,702
Divide by: Operating Ratio	<u>88%</u>
Sub-Total	112,161
Less: Pro Forma Operating Expenses Before Income Taxes	<u>(98,702)</u>
Allowable Net Operating Income	<u><u>\$ 13,459</u></u>

<sup>12</sup>

Operating Expenses	\$ 101,911
Divided by: Operating Revenues	<u>115,370</u>
Operating Ratio	<u><u>88.33%</u></u>

13. A flat monthly sewer service rate of \$34.71 is necessary to produce the required revenues.<sup>13</sup>

14. Joann Estates' proposed rate will produce annual revenues in excess of \$115,370 and should be denied.

15. Joann Estates calculated test year depreciation expense on certain assets using the double declining method. In all future reporting periods, Joann Estates shall report depreciation expense on all assets using the straight-line method as required by the Uniform System of Accounts.<sup>14</sup>

16. Joann Estates should, within 60 days of the date of this Order, refund to its customers with interest all amounts collected from February 22, 2014, through the date of this Order that are in excess of the rates that are set forth in Appendix B to this Order. Interest should be based upon the average of the Three-Month Commercial Paper Rate as reported in the Federal Reserve Bulletin and the Federal Reserve Statistical Release on the date of this Order.

IT IS THEREFORE ORDERED that:

1. The rate proposed in Joann Estates' Application is denied.
2. The rate shown in Appendix B is approved for sewer service rendered on and after February 22, 2014.

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<sup>13</sup>

Revenue Required from Rates	\$ 115,370
Divide by: Number of Customers	277
12 Months	<u>12</u>
Monthly Flat Rate	<u>\$ 34.71</u>

<sup>14</sup> Staff Report at 23.

3. Within 20 days of the date of this Order, Joann Estates shall file revised tariff sheets with the Commission, using the Commission's electronic Tariff Filing System, containing the rates set forth in Appendix B to this Order.

4. As agreed in response to Staff's report, Joann Estates shall expend \$9,600 annually for sludge removal in all future reporting periods; however, this amount is prorated to \$7,200 for the year ending December 31, 2014, since Joann Estates will not begin recovery of the sludge hauling expense until April, 2014, when the rates approved by this Order become effective. Joann Estates shall report all sludge hauling expenses using account 701-C (Labor and Expense, Treatment System, Sludge Hauling) when filing its Annual Financial and Statistical Reports with the Commission and it shall attach copies of all invoices that support the amount reported. The invoices shall clearly indicate the plant or lagoon from which sludge was removed.

5. In all future reporting periods, Joann Estates shall depreciate its assets using the straight-line method. No retroactive adjustment to accumulated depreciation or retained earnings shall be made to account for this change in accounting method.

6. Within 60 days of the date of this Order, Joann Estates shall refund to its customers with interest all amounts collected for service rendered from February 22, 2014, through the date of this Order that are in excess of the rates that are set forth in Appendix B to this Order.

7. Joann Estates shall pay interest on the refunded amounts at the average of the Three-Month Commercial Paper Rate as reported in the Federal Reserve Bulletin and the Federal Reserve Statistical Release on the date of this Order. Refunds shall be based on each customer's usage while the proposed rates were in effect and shall be

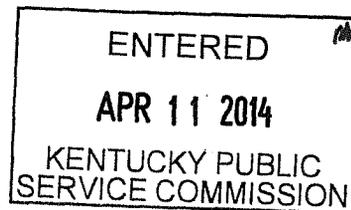
made as a one-time credit to the bills of current customers and by check to customers that have discontinued service since February 22, 2014.

8. Within 75 days of the date of this Order, Joann Estates shall submit a written report to the Commission in which it describes its efforts to refund all monies collected in excess of the rates that are set forth in Appendix B to this Order.

9. Any documents filed with the Commission pursuant to Ordering Paragraph 8 shall reference this case number and shall be retained in the utility's general correspondence file.

10. The Executive Director is delegated authority to grant reasonable extensions of time for the filing of any documents required by Ordering Paragraph 8 upon Joann Estate's showing of good cause for such extension.

By the Commission



ATTEST:

  
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Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 2013-00307 DATED **APR 11 2014**

Joann Estates Utilities, Inc.'s Adjusted Operating Statement

Operating Revenue	
Sewer Service Revenue	<u>\$ 115,370</u>
Total Operating Revenue	<u>115,370</u>
Operating Expenses	
Operation and Maintenance	
Owner/Manager Fee	3,600
Collection System	16,800
Treatment System - Sludge Hauling	9,600
Treatment System - Water Cost	15,366
Treatment System - Other	29,388
Rents	
Agency Collection Fee	11,537
Office Supplies and Other Expenses	89
Insurance Expense	4,815
Transportation Expenses	
Miscellaneous General Expenses	<u>1,868</u>
Total Operation and Maintenance Expenses	93,063
Amortization	2,004
Depreciation	2,056
Taxes Other Than Income	<u>1,579</u>
Total Operating Expenses Before Income Taxes	98,702
Income Taxes	
State Income Taxes	834
Federal Income Taxes	<u>2,375</u>
Total Operating Expenses	<u>101,911</u>
Net Operating Income	<u>\$ 13,459</u>

## APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 2013-00307 DATED **APR 11 2014**

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

### Monthly Sewer Rates

\$34.71 per residential equivalent

Destiny Hammond  
7510 Chiles Drive  
West Paducah, KENTUCKY 42086

Billy G Waid  
Owner  
JoAnn Estates Utilities, Inc.  
6500 US HWY 60 West  
Paducah, KY 42001