

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

ADJUSTMENT OF RATES OF AUXIER )  
ROAD GAS COMPANY, INC. OF ) CASE NO. 7897  
PRESTONSBURG, KENTUCKY )

O R D E R

On June 27, 1980, Auxier Road Gas Company, Inc., (Applicant), a natural gas distribution utility serving approximately 503 residential and commercial customers in Floyd County, Kentucky, filed a notice with the Energy Regulatory Commission (now the Public Service Commission) requesting an increase in rates for natural gas service to be effective on and after August 1, 1980. The proposed rates would produce additional annual revenues of \$69,972, an increase of approximately 20.0%. Applicant stated that the requested increase was necessary to meet the higher debt service and depreciation associated with its application to borrow monies from the federal Economic Development Administration through the Kentucky Department for Local Government gas reconstruction program in Case No. 7884.

To determine the reasonableness of the proposed rates, the Commission in an order dated June 30, 1980, suspended the requested increase in rates for a period of five (5) months on and after the effective date. Further, in an Order dated August 19, 1980, the Commission set a public hearing to be held November 6, 1980, at its offices in Frankfort, Kentucky. Notice of such hearing was made by Applicant in the manner prescribed by the Kentucky Revised Statutes

and the Commission's regulations.

A public hearing in this matter was held as scheduled with the Consumer Intervention Division of the Attorney General's Office being the only party to intervene. At the hearing, Applicant apprised the Commission that only a portion of its application to borrow monies from the Department for Local Government had been approved and it would be necessary to borrow additional monies to complete its reconstruction program. Further, Applicant stated that the record would be supplemented with additional documentation as it became available and that waiver of the five (5) month suspension period would be given. The Commission's Staff requested certain additional information at the hearing, and following responses to these requests and the supplementation of the record filed by Applicant on February 5, 1981, the matter was submitted to the Commission for final determination.

#### TEST PERIOD

For purposes of testing the reasonableness of the proposed rates and charges, the Commission has adopted the twelve months ended March 31, 1980, as the test period. Adjustments, where proper and reasonable, have been included to more clearly reflect current operating conditions.

#### VALUATION METHODS

##### Net Investment

On Exhibit 3 (Interim) of the notice, Applicant proposed an adjusted Net Investment Rate Base of \$460,825 and an additional \$50,008 in its supplementation of the record for a total of \$510,833.

The Commission agrees with Applicant's proposed rate base with the exception of the inclusion of the extraordinary property loss and the calculation of the cash working capital allowance, which in accordance with past policy, has been calculated as one-eighth of the adjusted operation and maintenance expenses less the cost of purchased natural gas. In addition, Applicant's proposed rate base has been reduced to exclude the balance of \$7,600 in Account 252, Customer Advances for Construction. Thus, the Commission has determined Applicant's Net Investment Rate Base at March 31, 1980, adjusted for its reconstruction program to be as follows:

Utility Plant in Service		\$501,126
Prepayments		5,445
Material and Supply Inventory		1,823
Cash Working Capital Allowance		9,576 <sup>(1)</sup>
Subtotal		<u>\$517,970</u>
Less:		
Accumulated Depreciation	\$41,143	
Customer Advances	<u>7,600</u>	
Total Deductions		48,743
Net Investment Rate Base		<u>\$469,227</u>

### Capital Structure

Applicant proposed a capital structure of \$459,513 per its Exhibit 3 (Interim) and proposed an amended capital structure of \$529,938 in its supplementation of the record filed February 5, 1981. The Commission has accepted the Applicant's proposed capital structure at the end of the test period as adjusted for its reconstruction program, as follows:

Equity:			%
Common Stock	\$ 20,000		3.8
Other Paid in Capital	2,035		0.4
Unappropriated Retained Earnings	<u>62,339</u>		11.7
Total Equity	\$ 84,374		15.9
Long-Term Debt	<u>445,564</u>		84.1
Total Capitalization	<u>\$529,938</u>		<u>100.0</u>

Although no other methods of valuation have been included

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<sup>(1)</sup> \$76,610 x 12.5% = \$9,576

herein, the Commission has given due consideration to all elements of value in order to determine the reasonableness of this matter.

REVENUES AND EXPENSES

Applicant proposed several adjustments to its Operating Statement to more closely reflect current operating conditions.<sup>(2)</sup> The Commission finds these adjustments to be proper, and they have been accepted for rate-making purposes with the following exceptions:

(1) In the adjustments to normalize test period natural gas sales and purchases and the net adjustment to revenues for temperature variance, Applicant applied the Columbia Gas Rate and the rates for natural gas service rendered as set out in Case No. 7521. Subsequent purchased gas adjustments have been granted by the Commission and therefore, in the above-mentioned adjustments, the Commission has applied the Columbia Gas Rate and the rates for natural gas service rendered by the Applicant as set out in Case No. 7521-F, the latest rates approved. Applicant's proposed adjustments and the adjustments found reasonable, as calculated in the same manner proposed by the Applicant with the exception of presenting gross adjustments to revenues and expenses for temperature variance rather than a net adjustment to revenues, have been set out in comparative form below:

	<u>Applicant's Proposal</u>	<u>Commission Accepted</u>	<u>Difference</u>
Adjustment to Normalize Natural Gas Sales	\$ 59,213 <sup>(3)</sup>	\$ 81,095	\$ 21,882
Adjustment to Normalize Natural Gas Purchases	\$ 38,304 <sup>(3)</sup>	\$ 60,193	\$ 21,889

(2) Applicant's Exhibit 2 (Interim), Page 2.

(3) Applicant's Exhibit 2 (Interim), Page 2.

	<u>Applicant's Proposal</u>	<u>Commission Accepted</u>	<u>Difference</u>
Adjustment for Temperature Variance - Revenue	\$ (5,374) <sup>(4)</sup>	\$(20,990)	\$(15,616)
Adjustment for Temperature Variance - Expense	\$ -0-	\$(16,121)	\$(16,121)

(2) Applicant proposed an adjustment to reduce operating revenues by \$9,000 to reflect nonrecurring revenues collected for extensions and other work performed for its customers. After numerous questions and information requests concerning the events and entries of record which occurred regarding this adjustment, the Commission has accepted the above amount as a proper adjustment to test period revenues. However, the Commission has made a corresponding adjustment to reduce operating expenses in the amount of \$7,600 as it was learned through inquiry that Applicant had debited Account 101, Plant in Service and credited Account 252, Customer Advances for Construction, for \$7,600 in an effort to capitalize these extensions. It was further learned that this adjusting entry was made subsequent to all original entries of record to revenue and expense accounts and that no reversals of these accounts were reflected. Accordingly, the Commission does not contend that \$7,600 was the proper amount to be capitalized nor that it is reflective of the total cost of the two extensions. However, it is the amount Applicant used in its entry and, therefore, is the amount used by the Commission. In addition, by allowing Applicant to reduce operating expenses some \$1,400 less than operating revenues, the Commission is in effect granting the Applicant the benefit of any

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(4) Applicant's Response to Commission Order filed October 29, 1980, Item 3.

doubt as to whether total costs of the extensions were in fact less than the amount received for construction.

(3) Applicant proposed adjustments for depreciation, interest and property tax expenses associated with its proposed gas reconstruction program. The Commission finds these adjustments to be generally proper although minor changes have been made in each of these adjustments. Following is a recapitulation of the changes:

(a) Depreciation expense has been reduced by \$1,619 for extraordinary retirements not excluded by the Applicant in its Exhibit 6 and further has been reduced \$138 when overhead costs associated with the reconstruction were allocated based on information in Applicant's supplementation of the record.

(b) Interest expense has been reduced by \$26 to a level required for a loan of \$445,564 at 5.125%.

(c) Property tax expense has been increased \$201 based on additional proposed plant in the amount of \$50,008 as provided in Applicant's supplementation of the record at the test period prevailing rate of \$ .40/\$100 of valuation.

(4) Applicant proposed to make an adjustment for estimated rate case expense of \$7,500<sup>(5)</sup>. Based on Applicant's historical rate case experience and Commission policy, this amount has been amortized over a three-year period. Therefore, Applicant's proposed adjustment has been reduced \$5,000 to an annual adjustment of \$2,500.

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(5) Applicant's Exhibit 2 (Interim), Page 2.

(5) The Commission has reduced the Applicant's test period operation and maintenance expenses by \$140<sup>(6)</sup> for contributions made to various charitable groups and organizations during the test period in accordance with past policy.

(6) Applicant proposed an adjustment to wages and benefits in the amount of \$20,203 for charges both to operating expense accounts and to other accounts, including amounts associated with capital items charged to Plant in Service subaccounts. The Commission finds this adjustment to wages and benefits to be generally proper. However, the Commission finds that only insignificant amounts of wages and benefits were capitalized during the test period<sup>(7)</sup> and that wages and benefits expensed during the test period associated with the two extensions should have been capitalized. Therefore, Applicant's proposed adjustment to wages and benefits has been reduced \$2,087<sup>(8)</sup> to reflect the proper reversal of those wages and benefits expensed inadvertently during the test period. The Commission further finds that Applicant should maintain sufficient time keeping records whereby proper amounts will be capitalized for wages and benefits when applicable.

Therefore, test year operations have been adjusted to produce the following results:

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(6) Applicant's Appendix 2 filed December 1, 1980

(7) Response 6 to Commission Order dated October 10, 1980

(8) Applicant's Appendix 5 including Applicant's adjustment for wages.

	<u>Actual Test Period</u>	<u>Pro Forma Adjustments</u>	<u>Adjusted Test Period</u>
Operating Revenue	\$303,172	\$ 51,105	\$354,277
Operating Expense	<u>292,759</u>	<u>77,223</u>	<u>369,982</u>
Operating Income	<u>\$ 10,413</u>	<u>\$(26,118)</u>	<u>\$(15,705)</u>

#### RATE OF RETURN

The Commission is of the opinion that a fair, just and reasonable rate of return on the Net Investment Rate Base should be 7.5% in that it will allow Auxier Road Gas Company, Inc., to pay its operating expenses, service its debt, and provide a reasonable surplus for equity growth. Thus, the adjusted operating deficit has been found to be clearly unjust and unreasonable. Therefore, test period operations result in a net operating income deficiency of \$50,897<sup>(9)</sup>. This deficiency adjusted for income taxes of \$2,340 would cause an additional revenue requirement of approximately \$53,237. Other gas revenues, penalties and sales tax commissions were increased proportionately with the higher level of revenues in the same manner as proposed by Applicant. Therefore, additional revenue requirements from natural gas sales would be reduced by \$577 to a level of \$52,660.

The Commission, after reviewing all the evidence of record and being advised, is of the opinion and finds:

- (1) That the proposed accounting treatment for net retirements of \$30,882 to Account 182, Extraordinary Property

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<sup>(9)</sup> \$469,227 x 7.5% = \$35,192 + \$15,705 = \$50,897



Losses, is in accordance with the Uniform System of Account prescribed for Natural Gas Companies, that the proposed amortization period of 10 years will allow the stockholders of Applicant opportunity to recover their investment and that the proposal should be approved.

- (2) That the schedule of rates and charges set forth in Appendix "A" is fair, just and reasonable for natural gas service rendered by Auxier Road Gas Company, Inc., in that, based on test period conditions, revenues of \$407,514 will be produced.
- (3) That the allowed rate of return on Net Investment Rate Base of 7.5% is fair, just and reasonable in that it should permit Auxier Road Gas Company, Inc. to pay its operating expenses, interest expenses and provide a reasonable amount of surplus for equity growth.
- (4) That the rates as proposed by Applicant and set out in the notice should be denied in that they will produce annual revenues in excess of those found reasonable herein.
- (5) That this Order combines all purchased gas adjustments approved by the Commission subsequent to the end of the test period and that they have been included in the natural gas service rates set out in Appendix "A".

IT IS THEREFORE ORDERED:

- (1) That the accounting treatment for net retirement of \$30,882 to Account 182, Extraordinary Property Losses, and its

amortization over a period of 10 years be and are hereby approved.

- (2) That the schedule of rates and charges set forth in Appendix "A" is fair, just and reasonable for natural gas service rendered by Auxier Road Gas Company, Inc., on and after the date of this Order.
- (3) That the rates proposed by the Auxier Road Gas Company, Inc., and set out in its notice, insofar as they differ from those in Appendix "A", shall be and are hereby denied.
- (4) That for the purpose of the future application of the Purchased Gas Adjustment Clause of Applicant the Base Rate for purchased gas shall be:

Commodity:

Columbia Gas of Kentucky, Inc.                      \$3.411 per MCF

- (5) That Auxier Road Gas Company, Inc., shall file with this Commission within thirty (30) days from the date of this Order its revised tariff sheets setting out the rates approved herein.

Done at Frankfort, Kentucky, this 23rd day of April, 1981.

PUBLIC SERVICE COMMISSION

Marlin M. Voh  
Chairman

• Did Not Participate  
Vice Chairman

Don Hanger  
Commissioner

ATTEST:

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Secretary

APPENDIX "A"

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE  
COMMISSION IN CASE NO. 7897 DATED

The following rates and charges are prescribed for the customers in the area served by Auxier Road Gas Company. 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 date of this Order.

Monthly Service Rates

First	1,000 cubic feet or less	\$6.00 (Minimum Bill)
All Over	1,000 cubic feet	\$5.20 per 1,000 cubic feet