

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

* * * *

In the Matter of:

AN ADJUSTMENT OF RATES OF)
CLEARVIEW WATER COMPANY, INC.) CASE NO. 7929

O R D E R

On July 30, 1980, Clearview Water Company, Inc. (Applicant), a utility engaged in the business of constructing, maintaining and operating a water distribution system for the purpose of furnishing water and water services for domestic, commercial and fire protection in a portion of the City of Danville and Boyle County, Kentucky, filed a petition with the Public Service Commission (formerly the Utility Regulatory Commission) requesting an increase in its rates for water and water service rendered. The proposed rates would produce additional annual revenues of \$20,275, an increase of approximately 40%. Applicant stated that the proposed increase was necessary in order that its capital investment and performance not be impaired because of an increase by its wholesale supplier, the City of Danville.

To determine the reasonableness of the proposed rates, the Commission, in an Order dated August 13, 1980, set a public hearing to be held December 16, 1980, at its offices in Frankfort, Kentucky. Notice of such hearing was made by Applicant in manners prescribed by the Kentucky Revised Statutes and the Commission's rules. A public hearing in this matter was held as scheduled with two parties intervening, the Consumer Intervention Division

of the Attorney General's Office and residents of Clearview Subdivision (Residents). At the hearing, the Residents' attorney moved for and was granted a continuance until January 20, 1981, in order that he be provided ample time in reviewing this matter. At the hearing on January 20, 1981, certain requests for additional information were made by the Commission Staff and following responses filed by Applicant on February 11, 1981, the matter was submitted to the Commission for final determination. Moreover, Applicant filed a notice with the Commission on January 23, 1981, having an effective date of February 15, 1981. On January 26, 1981, the Commission issued an Order suspending the rates proposed until May 30, 1981.

TEST PERIOD

For purposes of testing the reasonableness of the proposed rates and charges, the Commission has adopted the twelve months ended June 30, 1980, as the test period. Adjustments, where proper and reasonable, have been included to more clearly reflect current operating conditions.

VALUATION METHODS

Applicant's petition contained no exhibits setting forth its Net Investment Rate Base nor its Capital Structure and correspondingly, no proposed rates of return were projected. Furthermore, Applicant proposed no other valuation methods recognized by the Commission, but simply prepared a comparative income statement and projected, in Applicant's opinion, a reasonable profit.

Usually in privately-owned utilities such as this, it is Commission policy to review Applicant's Net Investment Rate Base, its Capital Structure and various other valuation methods when evaluating an Applicant's proposals. Since Applicant made no presentation of valuation methods, the Commission derived a reasonable method based on other information contained in the record of evidence, such as financial exhibits. However, Applicant stated that the financial exhibits filed with its petition were prepared on a "tax" basis rather than on a "book" basis as prescribed by the Uniform System of Accounts for Class C Water Utilities and the rules and regulations of this Commission. (1)

Generally, the principle difference between "tax" and "book" methods of accounting lies in the determination of depreciation expense as taxing authorities permit more rapid recovery of plant costs than regulatory agencies which in turn would provide a greater provision for accumulated depreciation and lower earnings for "tax" purposes when compared to "book" purposes. However, it can readily be seen when comparing Applicant's "tax" financial exhibits as filed and its "book" financial exhibits as shown in its Annual Report to the Commission adjusted for the same period that other significant differences are apparent, in particular plant in service and capital stock. Upon inquiry at the hearing, Applicant was unable to reconcile these differences. For purposes of this case only, the Commission has accepted the "tax" financial exhibits as filed. However, the Commission will

(1) Transcript of Evidence of January 20, 1981, page 92, responses 16 and 17.

not tolerate noncompliance with its rules and regulations in future petitions and recommends that a reconciliation between the two bases be completed and updated as needed. The Commission has determined that Applicant's Net Investment Rate Base and Capital Structure at the end of the test period as filed in its petition to be as follows:

Net Investment Rate Base

| | | |
|--------------------------------|------------|-----|
| Utility Plant in Service | \$ 140,133 | (2) |
| Cash Working Capital Allowance | 6,320 | |
| Subtotal | \$ 146,453 | |
| Less Accumulated Depreciation | 51,021 | (2) |
| Net Investment Rate Base | \$ 95,432 | |

The cash working capital allowance has been computed to be one-eighth of Applicant's adjusted operation and maintenance expenses. (3)

Capital Structure

| Equity: | | % |
|-------------------------------|-----------|----------|
| Common Stock | \$ 10,640 | 11.3 |
| Retained Earnings | 22,162 | 23.6 |
| Total Equity | \$ 32,802 | 35.0 (4) |
| Notes Payable to Stockholders | 61,000 | 65.0 |
| Capital Structure | \$ 93,802 | 100.0 |

Although no other methods of valuation have been included herein nor introduced by Applicant, the Commission has given due consideration to all elements of value in order to determine the reasonableness in this matter.

(2) Applicant's Balance Sheet as of June 30, 1980.

(3) \$50,560 X 12.5% = \$6,320.

(4) Rounding error.

REVENUES AND EXPENSES

Applicant proposed several adjustments to its Operating Statement to more clearly reflect current operating conditions.⁽⁵⁾ The Commission finds these adjustments to be proper and they have been accepted for rate-making purposes with the following exceptions:

(1) Applicant proposed an adjustment to legal and professional fees of \$3,500 for this rate request and ongoing litigation over water line rights. The record in this matter indicates that the \$3,500 adjustment is composed of two parts, first, \$1,000 for the estimated cost of this matter and secondly, \$2,500 for the estimated cost of attorneys' fees in the contract suit.⁽⁶⁾ The estimated rate case cost of \$1,000 has been amortized over a three-year period based on Applicant's historical rate case experience and Commission policy. Therefore, Applicant's proposed adjustment of \$1,000 has been reduced \$667 to an annual level of \$333.

(2) As indicated above, Applicant proposed an adjustment of \$2,500 for the estimated cost of attorneys in the contract suit presently in litigation in civil court. Further, the record in this matter indicates that \$750 of the actual test period expenses for legal and professional fees was associated with this ongoing litigation over water line rights,⁽⁷⁾ thus bring

(5) Applicant's Comparative Income Statement for the twelve months ended June 30, 1980.

(6) Transcript of Evidence of January 20, 1981, page 81, response 12.

(7) Transcript of Evidence of January 20, 1981, page 98, response 43.

the total legal fees associated with the contract suit to \$3,250. The Commission is of the opinion that these legal fees of \$3,250 are nonrecurring in nature and should be amortized over an extended length of time. Therefore, actual test period legal and professional fees have been reduced \$750 to a more normal level and the legal fees associated with the contract litigation have been amortized over five years or \$650 annually. Thus, inclusive of the above findings, the Commission finds reasonable legal and professional fees to be \$2,061.

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

| | <u>Actual Test Period</u> | <u>Pro Forma Adjustments</u> | <u>Adjusted Test Period</u> |
|----------------------|-------------------------------|----------------------------------|---------------------------------|
| Operating Revenue | \$ 51,451 | \$ 0 | \$ 51,451 |
| Operating Expense | <u>53,578</u> | <u>5,931</u> | <u>59,509</u> |
| Net Operating Income | <u>\$ (2,127)</u> | <u>\$(5,931)</u> | <u>\$ (8,058)</u> |

RATE OF RETURN

The Commission is of the opinion that a fair, just and reasonable rate of return on its Net Investment Rate Base should be 10.2% in that it will allow Clearview Water 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 and therefore, test period operations result in a net operating income deficiency of \$17,792.⁽⁸⁾ This deficiency, adjusted for

⁽⁸⁾ $\$95,432 \times 10.2\% = \$9,734 + \$8,058 = \$17,792$

income taxes of \$1,033, would cause an additional revenue requirement of approximately \$18,825.

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

(1) That, for purposes of future petition of this Commission, financial exhibits should be submitted as shown per Applicant's general ledger for "book" purposes and that a complete reconciliation between "book" and "tax" records should be completed and updated annually.

(2) That, for accounting purposes, billing and collection rendered by Applicant for Benedict Sewer Company should be maintained in a separate and independent manner, i.e., statements rendered Benedict should be directly paid by Benedict rather than deducted from sewer receipts collected by Applicant and then paid by Applicant.

(3) That the schedule of rates and charges set out in Appendix "A" are the fair, just and reasonable rates to charge for water and water service rendered by Clearview Water Company, Inc., in that, based on test period conditions, revenues of \$70,276 will be produced.

(4) That the allowed rate of return on Net Investment Rate Base of 10.2% is fair, just and reasonable in that it should permit Clearview Water Company, Inc., to pay its operating expenses, interest expense and provide a reasonable amount of surplus for equity growth.

(5) 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.

IT IS THEREFORE ORDERED:

(1) That, for purposes of future petition of this Commission, financial exhibits shall be submitted as shown per Applicant's general ledger for "book" purposes and that a complete reconciliation between "book" and "tax" records shall be completed and updated annually.

(2) That, for accounting purposes, billing and collection rendered by Applicant for Benedict Sewer Company shall be maintained in a separate and independent manner.

(3) That true copies of decisions and orders of the Boyle Circuit Court with regard to the ongoing contract suit shall be filed with this Commission within thirty (30) days of their receipt along with a statement by Applicant of their intentions regarding an appeal.

(4) That the schedule of rates and charges set forth in Appendix "A" are fair, just and reasonable for water and water service rendered by Clearview Water Company, Inc., on and after the date of this Order.

(5) That the rates proposed by Clearview Water Company, Inc., and set out in its notice, insofar as they differ from those in Appendix "A," shall be and are hereby denied.

(6) That Clearview Water 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 22nd day of April, 1981.

PUBLIC SERVICE COMMISSION

Marlin D. Cook
Chairman

Did not participate
Vice Chairman

Sam Harrison
Commissioner

ATTEST:

Secretary

APPENDIX "A"

APPENDIX TO AN ORDER OF THE PUBLIC
SERVICE COMMISSION IN CASE NO. 7929
DATED APRIL 22, 1981.

The following rates are prescribed for all general customers served by Clearview Water Company, 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 date of this Order.

GENERAL SERVICE RATES MONTHLY

| <u>Consumption Block</u> | <u>Monthly Rate</u> |
|--------------------------|------------------------|
| First 267 cu. ft. | \$ 5.30 (Minimum Bill) |
| Next 400 cu. ft. | 2.00 per 133 cu. ft. |
| Next 667 cu. ft. | 1.60 per 133 cu. ft. |
| Next 2,000 cu. ft. | 1.35 per 133 cu. ft. |
| Next 3,333 cu. ft. | 1.05 per 133 cu. ft. |
| Next 6,667 cu. ft. | .80 per 133 cu. ft. |
| Over 13,334 cu. ft. | .65 per 133 cu. ft. |
| | |
| Returned check charge | \$ 5.00 each check |