

COMMONWEALTH OF KENTUCKY
BEFORE THE UTILITY REGULATORY COMMISSION

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In the Matter of:

WILLOW UTILITIES, INC., FOR AUTHORITY)
TO ACQUIRE AND OPERATE THE WILLOW)
CREEK SEWER SYSTEM IN JEFFERSON AND)
OLDHAM COUNTIES, KENTUCKY)

AND) CASE NO. 7932

APPLICATION OF WILLOW UTILITIES, INC.)
FOR AN ORDER ADJUSTING THE RATES)
CURRENTLY CHARGED BY WILLOW CREEK)
SEWER SYSTEM)

ORDER

Preface

On July 31, 1980, Willow Utilities, Inc. ("Purchaser") and Pence Mortgage Company ("Seller") filed with the Commission a Joint Application seeking approval of the purchase and sale of the sewage treatment plant and system serving the Willow Creek Subdivision in Jefferson and Oldham Counties, Kentucky. Willow Utilities Inc. also filed, within the joint application, its proposal to increase sewer service rates presently being charged by the Willow Creek Sewer System.

The case was set for hearing at the Commission's offices in Frankfort, Kentucky, on November 11, 1980 at 9:00 a.m., Eastern Standard Time. All parties of interest were notified with the Consumer Intervention Division of the Attorney General's Office and Ms. D. Korfhage being permitted to intervene in the matter. At the hearing, certain requests for additional information were made by the Commission staff. This information has been filed, and the entire matter is now considered to be fully submitted for final determination by this Commission.

Test Period

The Applicant has selected the twelve month period ending April 30, 1980 as the "Test-Year" and has submitted tabulations of its actual revenues and expenses for this period including its pro-forma adjustments thereto for the Commission's consideration in the determination of a rate adjustment.

Valuation Methods

The Commission has found that the Utility's investment records are insufficient in detail to provide the necessary information to determine the net investment or capitalization of the Utility for rate making purposes. Therefore, the Commission is of the opinion that the "Operating Ratio Method" should be utilized in this instance.

The formula used in computing Operating Ratio is as follows:

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

Revenues and Expenses

Applicant proposed several adjustments to actual operating revenues and expenses as reflected in its Comparative Income Statement for the twelve months ended April 30, 1980. The Commission finds these adjustments allowable and has accepted them for rate-making purposes with the following exceptions:

1. Electricity Expense

Applicant's pro-forma electric expense adjustment was based on 155,117 KWH which was computed by averaging the last eight (8) months of the test period and annualizing same. (Ref.: Explanation of pro-forma adjustments to the Revised Comparative Income Statement, page no. two (2), item no. eight (8).) On November 17, 1980, the Commission received an addendum to the original adjustment of the Applicant in which KWH usage was itemized for the period September, 1979 through October, 1980. After reviewing this information, the Commission has computed average annual usage to be 147,035 KWH, using as a basis for this computation the twelve months ended October, 1980, to arrive at a projected annual cost of \$7,743.

2. Plant Maintenance & Repairs

Applicant proposed a pro forma level of plant maintenance and repairs expenses of \$4,919. This figure included an amortized level (\$1,833) of extraordinary repairs to be made to the system in the total amount of \$5,500. The liability for payment of this expense has become an issue in this case.

Mr. Marshall Parker, a representative of the Pence Mortgage Company, gave sworn testimony in the hearing of November 11, 1980, that the "seller" would bear the expense. Subsequent to the hearing, the Commission received a "letter-agreement" dated November 12, 1980 from Mr. Marshall to Mr. Cogan, president of Willow, which was initialed and acknowledged by Mr. Cogan. Essentially this document fixed the obligation for payment of \$4,250 of the total \$5,500 on the "purchaser" or Willow.

The Attorney General's Office filed a letter dated December 8, 1980, which objected to any consideration of the "letter agreement" as it was contradictory to the sworn evidence given in the Commission's hearing. The Applicant then filed a letter in response to the Attorney General stating among other things that liability for the extraordinary repairs had been discussed prior to the hearing but no agreement had been reached between the parties and, therefore, Mr. Parker had no alternative but to testify in the manner he did. However, the agreement was then made in the following week which firmly established the liabilities of the involved parties.

After consideration of the evidence concerning this issue, the Commission is of the opinion that as the case was filed on July 31, 1980, ample time was available for negotiations on the specific details of the sale. Therefore, the Commission finds that the sworn testimony in this case is the dominant evidence and must be the basis for any decisions reached. Therefore, the Commission has rejected the portion of these maintenance costs related to extraordinary repairs.

The Commission has, moreover, reduced maintenance expenses by \$325 for the cost of a power cable improperly included in this expense category. Pursuant to the testimony entered in this case the Commission has determined that this cost should properly be capitalized as it is a part of the "rebuilt aerator" and will have a useful life to the utility beyond the one-year period. Depreciation on this cable has been included as an expense herein as will be shown below.

Finally, the Commission has reduced the proposed maintenance expense by \$813. Of this amount \$752 is the amount of "inflation" that Applicant projected in this category. The Commission has rejected this as it is neither known or measurable. The remaining \$61 is not explained by the Applicant in any of the evidence of record and is therefore rejected on the same basis.

Following the above discussion the Commission has determined that the appropriate pro forma expense for plant maintenance and repairs is \$1,948.

3. Agency Collection Fees

Applicant proposed expenses for bill collection of \$1,332. The Commission has made an adjustment of \$111 to increase this expense to reflect the apportionment of the joint service cost of the collection agency (Louisville Water Company) for each bi-monthly bill of the customer which includes the charge for both water and sewer service ($\$1.36 \times 272 \times 6 \times 65\% = \$1,443$).

4. Insurance Expense

The pro-forma adjustment to Insurance Expense has been denied on the basis of not being a reasonable, known and measurable adjustment to test year expenses.

5. Depreciation Expense

Applicant proposed a pro-forma annual depreciation expense adjustment of \$3,342. The Commission, having evaluated all factors in the computation of this expense, considers the following to be allowable:

<u>Capital Item</u>	<u>Cost</u>	<u>Service Life</u>	<u>Depr. Rate</u>	<u>Expense</u>
Rebuilt Aerator	\$2,625	5 years	20%	\$ 525
Chlorine Cabinet-				
Air Maze Blower	672	10 years	10%	67
Power Cable	325	5 years	20%	65
Remaining Sewer Equipment	\$27,500	20 years	5%	<u>1,375</u>
Total				<u>\$ 2,032</u>

6. Income Taxes

The Federal and State corporate income tax liability of \$946 has been computed by the Commission on the basis of taxable income of \$4,852 and a composite tax rate of 19.49%.

Therefore, the following tabulation is the Commission's summary of "Test-Year" and adjusted annual revenues and expenses:

	<u>Actual⁽¹⁾ Expenses Test-Year</u>	<u>Pro-Forma⁽¹⁾ Requested</u>	<u>Pro-Forma Found Reasonable</u>
<u>Revenues:</u>			
Sewer Operating Revenues	\$ 15,451	\$ 40,383	\$ 34,794
<u>Expenses:</u>			
1. <u>Operation Expenses:</u>			
(a) Management Fee	-0-	1,200	1,200
(b) Sludge Hauling	1,070	1,260	1,260
(c) Utilities-Water	253	302	302
(d) Other-Water Analysis	70	200	200
(e) Utilities-Electric	6,352	8,168	7,743
(f) Chemicals	304	887	887
2. <u>Maintenance Expenses:</u>			
(a) Routine Maintenance Fee	4,270	5,100	5,100
(b) Maint. of Structures & Improvements	120	120	120
(c) Maint. of Treat. & Disposal Plt.	5,570	4,919	1,948
3. <u>Customer Accounts Expense:</u>			
(a) Agency Collection Fees	854	1,332	1,443
(b) Uncollectible Accounts	33	74	74
4. <u>Administrative & Gen'l. Expenses:</u>			
(a) Adm. & Gen'l. Salaries-Bookkeeping	-0-	1,200	1,200
(b) Outside Services Employed:			
Accounting-Recurring	-0-	350	350
Legal - Recurring	-0-	200	200
(c) Insurance Expense	551	734	551
(d) Regulatory Comm. Expense	50	50	50
(e) Rents-Office	-0-	600	600
5. <u>Other Expenses:</u>			
(a) Rate Case Expense:			
Accounting	-0-	500	500
Legal	62	562	562
Engineering	-0-	400	400
(b) Depreciation Expense	-0-	3,342	2,032
(c) Taxes Other Than Inc. Taxes	1,017	1,017	1,017
(d) Income Taxes-Fed. & State	-0-	820	946
Subtotal	\$ 20,576	\$ 33,337	\$ 28,685
6. Interest on Long-Term Debt	-0-	2,203	2,203
Total Expenses	\$ 20,576	\$ 35,540	\$ 30,888
Net Income (Loss)	\$ [5,125]	\$ 4,843	\$ 3,906

(1) "Actual" and "Pro forma Requested" income and expenses were taken from the Applicant's Comparative Income Statement (Revised 10/31/80) for the twelve-month period ending April 30, 1980.

Summary

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

1. That by the Joint Application filed July 31, 1980, Pence Mortgage Company has agreed to sell and Willow Utilities, Inc. has agreed to purchase the Willow Creek Sewer System which serves the Willow Creek Subdivision in Jefferson and Oldham Counties, Kentucky for a purchase price of \$27,500. The mode of payment consists of a ten (10) year promissory note to Pence Mortgage Company in the amount of \$27,500 at an interest rate of 10%.

2. That the Purchaser is ready, willing and able to provide for the operation and maintenance of the existing sewage treatment facilities in the area as set forth in the Application.

3. That the proposed sale of the Willow Creek Sewer System does not adversely affect the public interest and should be approved.

4. Within the scope of this joint application, the Purchaser proposes to increase sewer service rates presently being charged to customers of the Willow Creek Sewer System.

5. That the Purchaser should maintain a separate set of accounting records for each sewage treatment facility owned and operated by the Purchaser. That said records should conform with standard accounting procedures and be maintained in accordance with the Commission's Rules and Regulations.

6. That the Seller should file with the Commission within sixty (60) days of the date of this Order the appropriate journal entries effecting the sale of the Willow Creek Sewer System.

7. That the Purchaser should file with the Commission within sixty (60) days of the date of this Order the appropriate journal entries effecting the purchase of the Willow Creek Sewer System.

8. That, in this instance, the determination of rates and revenue requirements should be based on the operating ratio method.

9. That an operating ratio of .88 results from test-year operations, as adjusted, and it is considered fair, just and reasonable in that it will allow the Utility to pay its operating expenses, service its debt requirements and provide a reasonable surplus.

10. That the rates as prescribed and set forth in Appendix "A" attached hereto and made a part hereof should produce gross annual revenues of approximately \$34,794 from 272 customers and are the fair, just and reasonable rates to be charged for sewer service rendered by Willow Utilities, Inc. to customers located in the Willow Creek Subdivision, Jefferson and Oldham Counties, Kentucky.

11. That the rates proposed by the Applicant are unfair, unjust and unreasonable in that they would produce revenues in excess of those found reasonable herein and should be denied.

12. That the Applicant has filed with this Commission a valid third-party beneficiary agreement.

Orders in This Matter

The Commission, on the basis of the matters hereinbefore set forth and the evidentiary record in this case:

HEREBY ORDERS that Willow Utilities, Inc., be and is hereby authorized to purchase the Willow Creek Sewer System from the Pence Mortgage Company for the sum of \$27,500 as evidenced by the issuance of its ten (10) year promissory note for said amount at an interest rate of 10%.

IT IS FURTHER ORDERED that Willow Utilities, Inc. shall maintain a separate set of accounting records for each sewage treatment facility that is owned and operated by the Utility. Further, that said records shall conform with standard accounting procedures and be maintained in accordance with the Commission's Rules and Regulations.

IT IS FURTHER ORDERED that the Pence Mortgage Company shall file with the Commission within sixty (60) days of the date of this Order the appropriate journal entries effecting the sale of the Willow Creek Sewer System.

IT IS FURTHER ORDERED that Willow Utilities, Inc. shall file with the Commission within sixty (60) days of the date of this Order the appropriate journal entries effecting the purchase of the Willow Creek Sewer System.

IT IS FURTHER ORDERED that the rates prescribed and set forth in Appendix "A" attached hereto and made a part hereof be and they are hereby fixed as the fair, just and reasonable rates of Willow Utilities, Inc. for providing sewage disposal service to customers located in the Willow-Creek Subdivision of Jefferson and Oldham Counties, Kentucky, to become effective for service rendered on and after the date of this order.

IT IS FURTHER ORDERED that the rates sought by the Applicant be and the same are hereby denied.

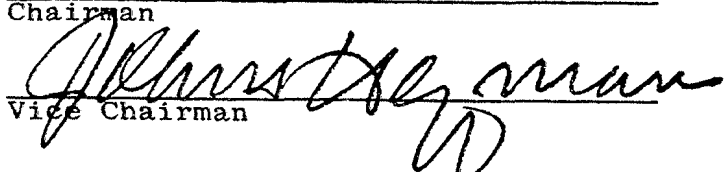
IT IS FURTHER ORDERED that the Applicant shall file with this Commission, within thirty (30) days from the date of this Order, its tariff sheets setting forth the rates approved herein. Further, that a copy of the Applicant's Rules and Regulations for providing service to its customers shall be filed with said tariff sheets.

Done at Frankfort, Kentucky, this 11th day of February, 1981.

UTILITY REGULATORY COMMISSION

Did not participate.

Chairman


Vice Chairman

Commissioner

ATTEST:

Secretary

APPENDIX "A"

APPENDIX TO AN ORDER OF THE UTILITY
REGULATORY COMMISSION IN CASE NO.
7932 DATED FEBRUARY 11, 1981.

The following rate is prescribed for sewage disposal service rendered to all customers served by Willow Utilities, Inc., in the Willow Creek Subdivision located in Jefferson and Oldham Counties, Kentucky.

<u>Type of Service Provided</u>	<u>Monthly Rate</u>
Single-Family Residential	\$ 10.66 per Single-Family Residence