COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

* * * * *

In the Matter of:

THE FILING OF A GENERAL RATE INCREASE BY LAKEWAY SHORES UTILITIES ASSOCIATION, INC.) CASE NO. 8502

O R D E R

On April 16, 1982, Lakeway Shores Utilities Association, Inc., ("Lakeway") filed its application with this Commission under 807 KAR 5:076 - Alternative Rate Adjustment Procedure for Small Utilities. The proposed rates would produce additional revenue of $1,944 annually, an increase of 60 percent based on normalized test year revenue.

A hearing was not requested in this matter and in accordance with the provision of the alternative rate adjustment procedure for small utilities no hearing was conducted. Therefore, the decision of the Commission is based on information obtained through written submissions.

COMMENTARY

Lakeway is a nonprofit water distribution system organized and existing under the laws of the Commonwealth of Kentucky, which serves approximately 54 customers in Calloway County.

TEST PERIOD

The Commission has adopted the 12-month period ending December 31, 1981, as the test period for determining the reasonableness of the proposed rates. In utilizing the historical test period, the Commission has given full consideration to known and measurable changes found reasonable.

REVENUES AND EXPENSES

Lakeway included a budgeted statement of expenses and a projected statement of income for 1982 in its application. Lakeway did not provide evidence in support of the budgeted level of revenues and expenses used in these statements nor an explanation as to how the amounts were determined. The Commission is of the opinion that these projected statements are extremely speculative in nature and not reasonably representative of future operations. The Commission in the past has allowed adjustments to the historical test year that are known and measurable. The Commission has consistently denied adjustments based on estimates and finds no compelling reason in this instance to depart from its past policy. Therefore, the Commission has not allowed these statements for rate-making purposes. The following adjustments have been made by the Commission to Lakeway's test period operating statement shown in its annual report for 1981:

Revenue Normalization

Lakeway's revenue for the test year was $4,552 which reflected actual cash receipts during the test year. Lakeway included in operating revenue an assessment of $40 per customer charged during the test year to pay for extraordinary expenses during 1981. The Commission is of the opinion that the income received from the assessment should not be included in revenue but should be recorded as contributions in aid of construction on the balance sheet. Therefore, the Commission has reduced test year revenue by $1,705 to exclude the income received from the assessment during the test year. The Commission has further adjusted test year revenue to $3,240 to reflect the annual revenue based on the level of customers and the rates in effect at the end of the test year.

School Taxes

The Commission has adjusted revenue and expenses by $95 to exclude school taxes erroneously charged to revenue and expense accounts during the test year. Operating revenue should be reported net of school taxes.

Public Service Commission Assessment

The Commission has increased Lakeway's tax expense by $50 for the assessment from the Public Service Commission. Lakeway did not incur an assessment fee during the test year because the Commission was not aware of its existence until November 1981.

Electric Expense

The Commission has adjusted test year electric expense to reflect the current rates in effect from Lakeway's electric supplier, West Kentucky Rural Electric Cooperative. In determining the pro forma electric expense the Commission has applied the current rates to the actual KWH used by Lakeway during the test year. This results in an adjusted electric expense of $1,064.

Repairs and Maintenance Expense

Lakeway incurred $1,148 of expense classified as repairs and maintenance during the test year for a new pump and motor. The Commission is of the opinion that these items should be capitalized and depreciated over the useful life of each item. However, Lakeway's test year included only $850 of the total expense because its financial reports are on a cash basis. Therefore, repairs and maintenance expense has been decreased by $850 to exclude the actual amount reported for the test year. In addition depreciation expense has been adjusted in accordance with the depreciation expense section of the Order.

Insurance Expense

Lakeway's insurance expense for the test year was $90 which reflected a 3-year premium from Murray Insurance Agency. The Commission is of the opinion that only the portion of the premium actually applicable to the test year should be reflected in insurance expense. Therefore, the Commission has reduced insurance expense by $60.

Chemical Expense

The Commission has reduced Lakeway's chemical expense by $169 to exclude $269 of expense reported in the test year that was actually incurred in 1980 and to include $100 for chemicals purchased but not paid for during the test year. Furthermore, the Commission has decreased chemical expense by $26 to reflect the correction of an amount erroneously recorded by Lakeway. The above adjustments result in an adjusted level of chemical expense of $642.

Salary And Wage Expense

Lakeway's salary and wage expense for the test year was $290. The Commission has included a total provision of $600 as the appropriate level of salary and wage expense for rate-making purposes herein.

Depreciation Expense

The Commission is of the opinion that the allowance for depreciation expense should be computed on the basis of the original cost of utility plant in service less accumulated contributions in aid of construction. Lakeway's original plant was contributed by Lakeway Shores Development Company ("Lakeway Development") in 1966 for $1. The original cost records were lost or destroyed when the original owners, Lakeway Development, went out of business. Therefore, Lakeway is currently carrying its plant at its appraisal value on the balance sheet because it does not have sufficient records to determine the original cost of the plant. The Commission does not approve of the appraisal value as a basis for valuation of plant. However, the Commission recognizes that the expense of conducting an original cost study to determine the proper valuation of plant would place an extreme financial burden on Lakeway.

Lakeway has no allowance for depreciation expense. Therefore, the Commission has established an allowance of $343 for depreciation expense as a result of the capitalization of certain items expensed by Lakeway for the calendar years 1980 and 1981. In determining the adjustment, the Commission has excluded contributions in aid of construction of $1,705 which is the amount collected from customers through the previously-mentioned special assessment. A detailed analysis of the Commission's adjustment to depreciation expense is included in Appendix B.

The Commission finds that Lakeway's adjusted test period operations are as follows:

	Actual Test Period	Pro Forma Adjustments	Adjusted Test Period
Operating Revenues	$ 4,552	$ (1,312)	$ 3,240
Operating Expenses	5,021	(265)	4,756
Operating Income	$ (469)	$ (1,047)	$ (1,516)
Interest Income	6	-0-	6
Net Income	$ (463)	$ (1,047)	$ (1,510)

REVENUE REQUIREMENTS

The Commission is of the opinion that the operating ratio(1) is a fair, just and reasonable method for determining revenue requirements in this case. The rates proposed by Lakeway will produce total revenues of $5,184 or an operating ratio of 92 percent. Therefore, the Commission is of the opinion that this level of revenue is not unreasonable and should be approved. The revenue allowed herein should be sufficient to pay Lakeway's operating expenses and improve its financial condition.

The Commission has made adjustments to reflect a normal level of revenue and expense on an accrual basis for rate-making purposes. Many of these adjustments were necessary to convert

(1) $\text{Operating Ratio} = \frac{\text{Operating Expenses + Depreciation + Taxes}}{\text{Gross Revenue}}$

Lakeway's annual operating revenue and expenses from the cash basis of accounting to the accrual basis. Therefore, in future rate proceedings under the alternative rate adjustment procedure, Lakeway should provide financial data under the accrual basis of accounting including depreciation for rate-making purposes. This Order should serve as a guide for Lakeway in its preparation of future rate case filings.

OTHER ISSUES

During the course of these proceedings the Commission learned that Lakeway has been charging unauthorized rates to its customers. The rate to these customers had been increased without the approval of the Commission. The Commission is of the opinion that a refund of the over collections at this time would place a severe financial burden on Lakeway which would have to be borne by all its customers. Therefore, the Commission finds that a refund would not be in the best interest of the customers of Lakeway and should not be required. Lakeway is hereby advised, however, that this Commission will not permit any future disregard of the law and may seek to impose the maximum statutory penalties if additional offenses occur.

SUMMARY

The Commission, after consideration of the evidence of record, finds that:

(1) The rates in Appendix A will produce gross annual operating revenue of $5,184 and are the fair, just and reasonable rates to be charged in that they will allow Lakeway to pay its

operating expenses and provide a reasonable surplus for equity growth.

(2) The rates proposed by Lakeway, insofar as they differ from those in Appendix A, should be denied.

(3) Lakeway does not have a a copy of its rules and regulations on file with the Commission as required by 807 KAR 5:011.

IT IS THEREFORE ORDERED that the proposed rates in Lakeway's application, insofar as they differ from those in Appendix A, be and they hereby are denied.

IT IS FURTHER ORDERED that the rates in Appendix A be and they hereby are approved for water service rendered by Lakeway on and after the date of this Order.

IT IS FURTHER ORDERED that within 30 days of the date of this Order, Lakeway shall file its revised tariff sheets setting forth the rates approved herein.

IT IS FURTHER ORDERED that Lakeway shall file an original and three copies of its rules and regulations with the Commission 30 days from the date of this Order.

Done at Frankfort, Kentucky, this 16th day of July, 1982.

PUBLIC SERVICE COMMISSION

Marlin M. Volz
Chairman

Katherine Randall
Vice Chairman

Commissioner

ATTEST:

Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE COMMISSION IN CASE NO. 8502 DATED JULY 16, 1982

The following rate is prescribed for all customers in the area served by Lakeway Shores Utilities Association, Inc.

Rates: Monthly

Single Family Residential	$8.00

APPENDIX B

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE COMMISSION IN CASE NO. 8502 DATED JULY 16, 1982

Calculation of Depreciation Expense

	Original Cost	Useful Life	Annual Depreciation Expense
1980 Plant Additions			
Drilling and Casing	$1,550	20	$ 78
Pump	650	10	65
Storage Tank	1,350	30	45
Chlorinator	113	10	11
Pump House	2,625	20	131
Subtotal	$6,288		$ 330
1981 Plant Additions:			
Pump and Labor	$ 823	10	$ 82
Motor	325	10	33
Subtotal	$1,148		$ 115
Total Plant Additions	$7,436		$ 445
Less: Contributions in aid of Construction	(1) 1,705		102
Total Depreciation allowed for Rate-making purposes			$ 343

(1) $\frac{\text{Contributions in Aid of Construction}}{\text{Total Plant Additions}} = \frac{\$1,705}{\$7,436} = 22.9\% \times$ Depreciation Expense ($445) = Contributed portion ($102)