COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

RATE ADJUSTMENT APPLICATION OF STONEBROOK SANITATION COMPANY, INCORPORATED, TO PUBLIC SERVICE COMMISSION USING ALTERNATIVE RATE FILING FOR SMALL UTILITIES	
THE AMENDED APPLICATION OF STONEBROOK SANITATION COMPANY, INCORPORATED, FOR CONSIDERATION OF A REQUEST FOR A CERTIFICATE OF CONVENIENCE AND NECESSITY TO CONSTRUCT IMPROVEMENTS TO EXISTING FACILITIES AND AUTHORITY TO BORROW FUNDS NECESSARY FOR SUCH PURPOSES	CASE NO. 8770
THE AMENDED APPLICATION OF STONEBROOK SANITATION COMPANY, INCORPORATED, FOR CONSIDERATION OF AUTHORITY TO BORROW FUNDS NECESSARY TO COMPLETE THE IMPLEMENTATION OF THE STOCK PURCHASE AGREEMENT BY THE COMMISSION IN CASE NO. 8676, DECEMBER 21, 1982	

O R D E R

On February 17, 1983, Stonebrook Sanitation Company, Inc., ("Stonebrook") filed an application with the Commission to increase its sewer rate pursuant to 807 KAR 5:076. On March 9, 1983, Stonebrook filed an amended application requesting a certificate of convenience and necessity to construct improvements to its existing facilities and authority to borrow approximately $25,000 at the current prime rate plus a maximum of two points

over prime for a period not to exceed 5 years. On August 4, 1983, Stonebrook filed its second amendment to the original application seeking authority to borrow funds necessary to complete the implementation of the stock purchase agreement previously approved by the Commission in Case No. 8676 on December 21, 1982.

Stonebrook requested a rate which would produce an annual increase of $30,384 to its present gross revenues. In this Order, the Commission has allowed a rate to produce an increase of $17,281.

Public hearings were held in this matter on May 31, 1983, and August 8, 1983, in the Commission's offices in Frankfort, Kentucky. The Consumer Protection Division of the Attorney General's Office and the Farmgate Homeowners' Association ("Farmgate") were permitted to intervene.

On September 15, 1983, Farmgate filed its brief in the case. All information requested by the Commission has been submitted.

MOTION TO DISMISS

An oral motion to dismiss Stonebrook's application was made by Mr. Carl J. Bensinger, counsel for Farmgate at the hearing on August 8, 1983. A written motion to dismiss was submitted and filed by Mr. Bensinger on September 15, 1983.

The three issues presented in Farmgate's motion are as follows:

1. Stonebrook has failed to perfect its application as amended by failure to submit a 1982 Annual Report.

2. The basic test period data (calendar year 1981) is "stale" and cannot form the basis for a decision on a rate increase.

3. A 1982 Annual Report or financial information no more than 90 days prior to the filing date is required even though a hearing has been held.

The Commission responds to Farmgate's concerns as follows:

1. The 1982 Annual Report of Stonebrook was filed in this Commission's offices on April 4, 1983.

2. The second issue is contingent on the first issue. Since the 1982 Annual Report has been filed, there is no basis for this argument.

3. Finally, Farmgate asserts that the financial data for the test year is beyond the 90-day requirement. The Commission in this instance has reviewed the 1981 and 1982 Annual Reports and finds no significant differences in financial position and, therefore, does not require Stonebrook to update its test year as no compelling reason to do so exists.

Therefore, the Commission is of the opinion that there are no valid reasons to support Farmgate's motion to dismiss and the motion should therefore be denied.

TEST PERIOD

For the purpose of determining the reasonableness of the proposed rates, the 12-month period ending December 31, 1981, has been accepted as the test period.

REVENUES AND EXPENSES

Stonebrook incurred an actual net loss for the test period of $4,023. Stonebrook proposed several pro forma adjustments to its test period operating revenues and expenses to more accurately reflect current operating conditions. The Commission finds these adjustments reasonable and has accepted them for rate-making purposes with the following exceptions:

Operating Revenues

Stonebrook reported gross revenues of $47,699 in its 1981 Annual Report, which erroneously included gross revenues of $3,059 for service rendered during 1980, outside the test period. The Commission agrees with Stonebrook in that adjusted actual gross revenues for services rendered during 1981 of $44,640 are the proper revenues to use for rate-making purposes.

Other Labor, Materials and Expenses

Stonebrook's recorded expense for other labor, materials and expenses for the test period was $1,050. This account is composed of NPDES quarterly testing of effluent by Bio-Chem of $400, the Louisville and Jefferson County Department of Health fee of $600 and a charge for a laboratory test made by Beckmar Lab on December 30, 1980, which was incurred by the previous owners but paid by Stonebrook during the test period. The Commission is of the opinion that the December 1980 lab test of $50 should be deleted from test period expenses as it is outside the test period.

Purchased Power Expense

Stonebrook projected purchased power expense of $9,905 for the test period on the basis of annualizing its actual electric cost for the first 8 months of 1982. Stonebrook's projection of $9,905 was further substantiated by the submission of its 1982 electric bills totaling $9,880 filed with the Commission on May 2, 1983.

In its response to the Commission's request for additional information received on August 19, 1983, Stonebrook requested an additional 7.51 percent increase to its projected power cost as a result of the rate increase granted to its electric supplier, Louisville Gas and Electric Company ("LG&E"), in Case No. 8616 entered by the Commission on March 3, 1983.

The Commission is of the opinion that projected power expense of $9,905 is reasonable and should be accepted for rate-making purposes and further that this amount should be increased by $744[1/] to reflect the recent rate increase granted LG&E.

Chemicals

Stonebrook projected chemical expense of $2,349 for the test period which included $400 for drum deposits. Drum deposits are refundable and are not an operating expense. Therefore, the Commission has denied this portion of Stonebrook's test period expense for chemicals.

Miscellaneous Supplies and Expenses-Treatment and Disposal

Stonebrook's test period expenses included $455 for miscellaneous supplies used in its treatment facility. A vendor

invoice of Suburban Sanitation Company dated July 1, 1981, indicated that Stonebrook was provided the use of a large dumpster to remove trash from the treatment plant area. Stonebrook, in its response to the Commission's request for additional information dated May 31, 1983, stated that this service would not be an annual recurring expense. The Commission is, therefore, of the opinion that $395 should be deleted from this account and transferred to an amortization expense account for proper amortization.

Routine Maintenance Service Fee

The initial contract between Stonebrook and Andriot-Davidson Service Company, Inc., ("Andriot-Davidson") which sets out a monthly fee of $400 per month for routine maintenance service to be performed by Andriot-Davidson, appears to be reasonable and has been allowed by the Commission for rate-making purposes.

Maintenance of Treatment and Disposal Plant

An analysis of individual invoices related to the maintenance of the treatment and disposal plant totaling $5,592 showed that during the test period Stonebrook made plant additions of $2,574[2/] to its sewer system and erronously expensed these items. These items will be given proper consideration by the Commission with regard to allowable depreciation expense.

Moreover, the Commission has also deleted from this account the cost of repairing the access road to the treatment plant of $302,[3/] cutting trees in the same area of $250[4/] and the cost of a survey of the manholes in the subdivision with regard to

infiltration of $537,[5] as they are considered non-recurring in nature. The Commission is of the opinion that these three items should be amortized over a reasonable period.

Agency Collection Fee

Stonebrook projected expenses related to the collection of the bi-monthly sewer bill by the Louisville Water Company of $2,267. The Commission has made an adjustment of $453[6] to increase this expense to reflect the apportionment of the joint service cost of the collection agency for each bimonthly bill of the customer which includes the charge for both water and sewer service.

Office Supplies and Other Expense

The Commission, after a review of the invoices representing office supplies and other expense for the test period, has transfered two items of expense to an amortization account for proper disposition as they are non-recurring expenditures. The review indicated that Stonebrook paid $359 to the George Marr Company (Invoice No. 20733) for duplicating its sewer system plans on file with the Jefferson County Board of Health. In addition, Andriot-Davidson purchased a copy machine and allocated $238 to Stonebrook as its portion of the cost of the joint ownership in the copying machine.

Miscellaneous General Expenses

During the test period Stonebrook paid an insurance premium of $325 to the Commonwealth Land Title Insurance Company for the purpose of insuring the title and integrity of the property in the transfer of ownership in January, 1981. Item No. 7 of

Stonebrook's response to this Commission's request for additional information received May 31, 1983, stated that this would not be a recurring expense and the Commission is of the opinion it should be amortized over a reasonable period. Therefore, the Commission has deleted $325 from miscellaneous general expenses.

Rate Case Expense

In the original application, Stonebrook included a pro forma adjustment of $900 amortized over a 3-year period related to the preparation of the ARF application by Automated Financial Service. Stonebrook, in its response of August 19, 1982, to the Commission, stated that it had incurred additional accounting and legal expense as a result of having two hearings in the Commission's offices in Frankfort, Kentucky. Automated Financial Service projected its additional filings and its attendance at the two hearings to be $750. Stonebrook employed Mr. W. H. Spalding III to represent it at the hearings and to attend to other legal matters pertaining to the rate case at a projected cost of $650. The Commission has determined that the additional rate case expense is allowable and has amortized the total cost of $2,300 over a 3-year period, allowing the inclusion of $767 as a pro forma operating expense.

Amortization Expense

The Commission, pursuant to its examination of invoices contained in various other test period operating expense accounts, found that Stonebrook incurred several items of expense as explained above, which are classified as being non-recurring in

nature. The Commission is of the opinion that Stonebrook should be allowed to amortize these non-recurring items over a 3-year period and has included $802[7] in test period expense.

Depreciation Expense

Farmgate in its brief proposed that the Commission disallow a portion of the depreciation expense associated with the original plant. When the plant was transferred to the current owner, the valuation of assets was $124,497. No specific breakdown of the assets was available as the original records were inadequate. Prior to sale, the depreciated utility plant cost on the books of Stonebrook was approximately $337,388.

Farmgate's position is that since no breakdown of the assests is available and the plant is situated on a parcel of land which Farmgate estimates to be worth $20,000, depreciation on that portion of the total plant cost should be disallowed. Stonebrook contends that the land was valued at $1.

The Commission has examined Stonebrook's 1981 federal income tax return and finds that the full value of the plant of $124,497 is being depreciated for tax purposes. Thus, Stonebrook's treatment of the property is consistent for book and tax purposes. Moreover, as the original booked cost is so far in excess of the new booked cost and no detailed breakdown of the transferred assets can be readily determined, the Commission is of the opinion that to allow depreciation expense on the full value of the transferred plant of $124,497 is reasonable and should be accepted for rate-making purposes.

At the end of the test period, Stonebrook had recorded depreciation expense of $12,515. Stonebrook had contributions in aid of construction of $1,000 at December 31, 1981. It is the policy of this Commission to disallow recovery on plant provided by the ratepayers. Therefore, depreciation expense has been reduced on the basis of recovered plant of $1,000 at the composite depreciation rate of 10 percent.

The Commission, in its disallowance of capital items of $2,574 included in the cost of maintaining the treatment and disposal plant as discussed above, has allowed a pro forma depreciation expense adjustment of $858 computed on the basis of a 3-year service life of the property which is properly transferred to Account No. 373, Treatment and Disposal Equipment. Moreover, the Commission has allowed an additional pro forma depreciation expense adjustment of $2,407 based on gross plant additions (approved by the Commission herein) of $24,070 with a useful life of 10 years. The Commission is of the opinion that the major additions to the original treatment plant would add a minimum of 10 years to the life of the property. Therefore, the Commission finds that reasonable adjusted depreciation expense for the test period is $15,680[8/] for rate-making purposes.

Interest on Long Term Debt

Stonebrook incurred interest on long term debt of $6,088 during the test period. Stonebrook proposed a pro forma interest expense adjustment of $4,338 based on a proposed loan of $24,100 at an interest rate of 18 percent for the purpose of paying Andriot-Davidson for the reconstruction of the concrete plant.

This plant was constructed prior to the filing of this case. However, the Commission has evaluated the evidence and finds that the plant additions are necessary and are in the public interest.

The Commission recognizes that Stonebrook will be required to borrow the funds for the completed additions through a bank or other lending institution. However, it is the Commission's policy not to grant pro forma adjustments which are neither known nor measurable. Therefore, the Commission must deny this proposed interest expense at this time. In the event that Stonebrook is able to obtain a commitment from a bank or other lending institution for a loan with a stipulated rate of interest for the financing required and other lending terms to pay for the completed construction and submit proof thereof within 20 days of the date of this Order, the Commission will be receptive to a rehearing on this matter.

Income Taxes

Stonebrook projected pro forma federal and state corporate income taxes, and the Jefferson County Occupational tax totaling $2,250 for the test period. Stonebrook's 1981 federal tax return showed a 10 percent investment tax credit of $9,000 based on property valuation of $90,000 which was assigned to Stonebrook. Investment credit of $429 was applied to the taxable year 1981 with an investment credit carry-over available for application to future years of $8,571. The Commission is of the opinion that Stonebrook's ratepayers should receive benefit from this investment tax credit as a result of the investment tax credit of

Stonebrook being applied to future taxable years. Stonebrook did not defer this credit nor propose any treatment to reduce tax expense for the credit. It is therefore the Commission's opinion that since the magnitude of the carry-over should be sufficient to reduce a federal tax expense to zero for the period these rates are in effect, unless financial conditions should substantially change, no federal tax expense will be allowed for rate-making purposes. The Commission is further of the opinion that the Kentucky Corporate Income Tax and the Jefferson County 2.2 percent Occupational tax should be allowed for rate-making purposes and will be computed in a later section of this Order.

Therefore, Stonebrook's adjusted operations at the end of the test period are as follows:

	Stonebrook Adjusted	Commission Adjustments	Commission Adjusted
Operating Revenues	$ 44,640	$ -0-	$ 44,640
Operating Expenses	55,577	(6,804)	48,773
Net Operating Income	$ (10,937)	$ 6,804	$ (4,133)
Interest Expense	10,426	(4,338)	6,088
Net Income	$ (21,363)	$ 11,142	$(10,221)

REVENUE REQUIREMENTS

The Commission is of the opinion that Stonebrook's adjusted operating loss is unfair, unjust and unreasonable. The Commission is further of the opinion that an operating ratio of 88 percent is fair, just and reasonable in that it will allow Stonebrook to meet its operating expenses, service its debt and provide a reasonable return to its stockholders. Therefore, the Commission finds that Stonebrook should be permitted to increase its rate to produce an

increase in annual revenue of $17,281,[9] which includes state and Jefferson County income taxes of $360.

OTHER ISSUES

On August 4, 1983, Stonebrook amended its rate application and requested permission to borrow funds for the purpose of completing implementation of the stock purchase agreement previously approved by the Commission in its Order in Case No. 8676, An Investigation of the Transfer of Ownership and Control of Stonebrook Sanitation Company, Inc., dated December 21, 1982.

Case No. 8770 was filed on February 17, 1983, for the primary purpose of determining an adjusted rate to charge the customers of Stonebrook for sewer service. This motion to amend this case is both untimely and not specifically related to rate-making purposes. Moreover, the August 8, 1983, hearing in this case did not give the intervenors nor the Commission sufficient time to thoroughly examine this evidence.

This issue is directly related to Case No. 8676. Therefore, the Commission will not consider this request in this case but instructs Stonebrook to file a motion and all related evidence to either re-open Case No. 8676 or to file an application for financing consistent with the Commission's regulations.

SUMMARY

The Commission, after consideration of the evidence of record and being advised, is of the opinion and finds that:

1. The rate proposed by Stonebrook would produce revenues in excess of the revenues found reasonable herein and should be denied upon application of KRS 278.030.

2. The rate in Appendix A is the fair, just and reasonable rate to charge for sewer service rendered to Stonebrook's customers and should produce annual revenues of approximately $61,921.

3. Stonebrook has on file with this Commission a valid third-party beneficiary agreement.

4. The reconstruction of the original concrete treatment plant at a cost of approximately $24,000 is both necessary and in the public interest in that it will aid Stonebrook with the problems of infiltration, and furthermore it should not create any sizable amount of excess capacity.

5. The amendment of Stonebrook to this rate application concerning financing of the stock purchase agreement should be denied and refiled for consideration as a part of Case No. 8676 or as a new financing case.

IT IS THEREFORE ORDERED that the rate in Appendix A be and it hereby is fixed as the fair, just and reasonable rate of Stonebrook for sewer service rendered on and after the date of this Order.

IT IS FURTHER ORDERED that the rate proposed by Stonebrook be and it hereby is denied upon application of KRS 278.030.

IT IS FURTHER ORDERED that the reconstruction of the concrete plant be and it hereby is approved.

IT IS FURTHER ORDERED that Stonebrook's motion to amend its filing to request permission to borrow funds for its stock purchase be and it hereby is denied.

IT IS FURTHER ORDERED that, within 30 days of the date of this Order, Stonebrook shall file with this Commission its tariff sheets setting forth the rate approved herein and a copy of its rules and regulations for providing sewer service.

Done at Frankfort, Kentucky, this 3rd day of November, 1983.

PUBLIC SERVICE COMMISSION

Chairman

Vice Chairman

Commissioner

ATTEST:

Secretary

FOOTNOTES

1. $9,905 X 7.51 percent = $744.

2. Invoices supplied in response to the Commission's Order dated March 16, 1983.

Invoice No.	Item	
407-4	New clocks and space heaters + installation	$ 313
529-2	Rebuild variable speed pump and grinder	1,384
706-5	Install barksdale pressure switch	112
416-2	Replace copper tubing in circulating line	587
1230-37	Install 110-V outlet and new space heater	178
	Total	$2,574

3. Invoices supplied in response to the Commission's Order dated March 16, 1983. (Invoice Nos. 1207-3 and 61916.)

4. Ibid. (Invoice No. 407-4.)

5. Ibid. (Invoice No. 1230-37.)

6. $1.72 X 65.9 percent X 400 X 6 = $2,720 - $2,267 = $453.

7. $2,406 ÷ 3 years = $802.

8.

	Depreciation Expense, Per books at 12/31/81	$12,515
Deduct:	Depreciation Expense on Contributions In Aid of Construction of $1,000 X 10 percent.	(100)
Add:	Depreciation expense on capital items transferred from maintenance of treatment plant - $2,574 X 33.33 percent.	858
	Pro forma depreciation expense on capital additions to the treatment plant of $24,070 X 10 percent.	2,407
	Total allowable depreciation expense	$15,680

9. ($48,773 + $360) ÷ 88 percent = $55,833 + $6,088 - $44,640 = $17,281.

APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE COMMISSION IN CASE NO. 8770 DATED NOVEMBER 3, 1983

The following rate is prescribed for customers receiving sewer service from Stonebrook Sanitation 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 effective date of this Order.

CUSTOMER CLASS	RATE
Single family residential	$12.90 per month