

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

THE APPLICATION OF WINDSOR)
FACILITIES INC., D/B/A WINDSOR)
FOREST SEWER SYSTEM FOR AN) CASE NO. 9138
ADJUSTMENT OF RATES PURSUANT TO)
THE ALTERNATIVE PROCEDURE FOR)
SMALL UTILITIES)

O R D E R

On September 14, 1984, Windsor Facilities, Inc., D/B/A Windsor Forest Sewer System ("Windsor") filed an application with the Commission to increase its sewer rates pursuant to 807 KAR 5:076. This regulation allows utilities with 400 or fewer customers or \$200,000 or less gross annual revenues to use the alternative rate filing method ("ARF") in order to minimize the necessity for formal hearings, to reduce filing requirements and to shorten the time between the application and the Commission's final Order. This procedure should minimize rate case expenses to the utility and, therefore, should result in lower rates to the rat@payers.

There were no intervenors in this matter, and all information requested by the Commission has been submitted.

Windsor requested rates which would produce an annual increase of \$31,584 to its present gross revenues. In this Order, the Commission has allowed rates to produce an increase of \$16,643.

TEST PERIOD

For the purpose of determining the reasonableness of the proposed rates, the 12-month period ending December 31, 1983, has been accepted as the test period.

REVENUES AND EXPENSES

Windsor showed a net loss on its books for the test period of \$18,277. Windsor 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:

Water Expense

During the test period, Windsor incurred water expense of \$1,421. The Louisville Water Company announced in the month of December 1984 that rates for water service would be increased by 7.2 percent effective January 1, 1985. Therefore, the Commission finds it appropriate to make a pro forma adjustment to water expense of \$102.¹

Purchased Power Expense

The Commission has reduced Windsor's adjusted purchased power expense for the test period of \$15,826 by \$53. Windsor erroneously included purchased power expense of \$85 for the month of December, 1982, in its test period expense. Moreover, the Commission also finds it appropriate to increase this operating expense by \$1,136, which represents the 7.76 percent increase

¹ $\$1,421 \times 7.2\% = \$102.$

granted the Louisville Gas and Electric Company in its last rate case before the Commission (Case No. 8924), granted subsequent to the test period in this case. Therefore, the Commission has included adjusted purchased power expense of \$15,773 in test year expenses.

Chemical Expense

Windsor had chemical expense of \$943 for the test period. An Ulrich Chemical, Inc., invoice (no. 5002670) in the amount of \$104.37 shows that a drum of chemicals was purchased by Windsor on December 4, 1980, prior to the test period. This cost was inappropriately included in test year expenses and therefore, the Commission has reduced chemical expense by \$104.37.

Routine Maintenance Service Fee

Windsor reported Routine Maintenance Service Fees of \$7,800 paid during the test period to Andriot-Davidson's Service Company, Inc. ("Andriot-Davidson"). In Windsor's previous rate order, Case No. 8112, dated August 7, 1981, the Commission allowed an expense level for routine maintenance of \$3,684 to be included in operating expenses for rate-making purposes. In response to the Commission's request for additional information dated September 27, 1984, Windsor furnished the Commission a copy of the contract negotiated with Andriot-Davidson for services rendered during the test period at a monthly fee of \$650 per month, or an increase of \$343 per month over the amount allowed in the previous rate case. In considering this adjustment, the Commission determined that transactions between Windsor and Andriot-Davidson, because of their mutual ownership, by Mr. Carroll Cogan, are not at

arms-length and, therefore, the burden of proof is on Windsor to demonstrate that the increase of \$343 per month paid to Andriot-Davidson for routine maintenance service is fair, just and reasonable. In order to determine the reasonableness of the increased maintenance fee, the Commission requested detailed information regarding the services provided, the basis of the monthly fee and comparative data for other plants served by Andriot-Davidson. The response to this request did not adequately identify the increased level of services provided to justify the increase above that level previously allowed.

It is the Commission's opinion that Windsor has not met its burden of proof on this issue and the adjustment from \$307 to \$650 per month should not be allowed for rate-making purposes in this case. Therefore, the Commission has made an adjustment to reduce the reported test year expense of \$7,800 by \$4,116 which reflects a routine maintenance service fee of \$3,684 annually. In making this adjustment, the Commission recognizes that this case was an ARF proceeding in which a hearing was not held. Therefore, Windsor is hereby apprised that the Commission will consider a motion for a formal hearing on this matter should Windsor indicate that it intends to submit persuasive proof in support of its test year expense for routine maintenance service.

Maintenance of Treatment and Disposal Plant

During the test period Windsor booked \$11,467 in maintenance of its treatment and disposal system. An analysis of the individual invoices showed that, during the test period, Windsor made a plant addition of \$4,106 to its sewer system for

the purpose of re-building a collector as evidenced by Andriot-Davidson's invoice No. 1114-4 dated November 14, 1983. This capital item was inappropriately included in test year expenses. The Commission has also removed from test year operating expenses services rendered by Andriot-Davidson on October 5, 6 and 8, 1982, of \$304 as evidenced by their Invoice No. 111-37 dated January 11, 1983, as these costs pertain to periods outside the test year. The following non-recurring items related to the maintenance of property damaged by Windsor have been removed from test year expenses and amortized over 3 years:

<u>Invoice No.</u>	<u>Date</u>	<u>Vendor</u>	<u>Amount</u>
1114-4	11/14/83	Andriot-Davidson's Service Company, Inc.	\$ 675.21
-	5/31/83	Seeding and Sodding Company, Inc.	91.00
9566	-	Greg Schneider	<u>400.00</u>
Total			\$1,166.21

Therefore, test period expenses related to the maintenance of the treatment and disposal system have been reduced by a total of \$5,576 to \$5,891. Depreciation and amortization expense on the above items will be discussed later in this Order.

Collection Expense

The collection expense is directly related to the amount of revenue that Windsor collects via the formula used by the Louisville Water Company ("LWC") to calculate the collection

charge.² Therefore, the Commission has modified this calculation to include the increased rate allowed herein. The Commission is also using the most recent collection fee charged by the LWC effective May 1, 1984, which results in an annual collection expense of \$2,587, an increase of \$925.

Insurance Expense

Windsor incurred insurance expense for the test period of \$740. At the Commission's request, Windsor provided copies of its test year insurance invoices for examination.³ An invoice of E. O. Mershon, Jr. & Associates shows a pro-rata allocation of \$220 to Windsor of a \$4,620 premium for a life insurance policy on Mr. Carroll Cogan. The Commission takes judicial notice that the named beneficiary in the policy is the estate of Carroll F. Cogan⁴ and, therefore, it is of the opinion that the pro-rata portion of the life insurance premium should be borne by the stockholders. Thus, the Commission has reduced test period insurance expense by \$220.

Transportation Expense

Included within Windsor's test-year operation and maintenance expenses are transportation charges in the amount of \$209. In support of this amount, Windsor provided an undated

² $\$1.80 \times \frac{\text{Sewer Charge}}{\text{Water Charge} + \text{Sewer Charge}} \times \text{No. of customers} \times 6.$

³ Response dated November 2, 1984, Item No. 6.

⁴ Response of Prairie Facilities, Inc., dated November 14, 1984, Item No. 4, in Case No. 9136--The Application of Prairie Facilities, Inc., D/B/A Prairie Village Sewer System, For An Adjustment of Rates Pursuant to the Alternative Procedure for Small Utilities.

invoice from Carroll Cogan Companies, Inc., ("CCC") for \$280⁵ which differs from the recorded amount on the records of Windsor. The documentation on the invoice shows 8 plant inspection trips and 1 trip to the health department, at \$35 per trip.

Because they are mutually-owned companies, it is the Commission's opinion that the transaction for car rental between CCC and Windsor is a less-than-arms-length transaction. Therefore, the burden of proof is on Windsor to establish justification for the expense. Moreover, reasonable expenses have been allowed in this case for outside service companies to maintain the plant on a routine and non-routine basis. Substantially, all transportation to and from Windsor for routine maintenance, sludge hauling and non-routine maintenance is provided for either within a monthly fee or billed by vendors on a per-mile basis. No basis as to the necessity or purpose of the additional travel by Mr. Cogan has been provided and, therefore, the expense should be disallowed.

Furthermore, it is the Commission's opinion that the cost of travel by Mr. Cogan for trips to the Windsor plant site is included as a part of the monthly fee paid to Andriot-Davidson for routine maintenance. Mr. Cogan is an employee of Andriot-Davidson and visits by him to the plant site are properly construed as travel by him in his capacity as a representative of Andriot-Davidson providing routine maintenance. And, as the contract for routine maintenance between Windsor and Andriot-Davidson makes no

⁵ Response dated November 2, 1984, Item No. 5a.

provision for additional payments for travel, the charges for transportation are inappropriate.

It is the Commission's policy to allow managers of sewer utilities of the size of Windsor annual compensation of \$1,800, including ordinary travel expenses. Additional compensation, such as for unusual travel expenses, must be sufficiently documented and justified. It is the Commission's finding that Windsor has not met its burden of proof on this issue and the Commission has therefore eliminated reported test-year transportation expense of \$209 from operating expenses for rate-making purposes.

Miscellaneous General Expenses

During the test period, Windsor incurred finance charges of \$727 from Andriot-Davidson. The finance charge is based upon 1-1/2 percent of the outstanding balance payable to Andriot-Davidson at the end of each month and is reported in Account 930, Miscellaneous General Expense. In this instance, the amount billed by Andriot-Davidson was for the period June 30 through November 30, 1983.

The Commission has reviewed the request to recover these finance charges in this case. Commission records indicate that Windsor last received rate relief in August, 1981. In the period subsequent to the Commission's decision in that case, Windsor's financial condition has deteriorated to the point that it could no longer remain current on its payments to vendors. Obviously, Windsor's failure to request rate relief while this situation developed is a material reason the finance charges have reached their current level. The burden of obtaining sufficient revenues

to pay operating costs clearly rests with the management of Windsor. The failure of Windsor to seek sufficient revenues to cover its operating costs in prior periods does not justify the request in this case to recover these costs from the present ratepayers. To allow Windsor to recover the cost of financing operations of prior years would constitute retroactive rate-making. Therefore, the Commission has excluded the finance charges of \$727 for rate-making purposes herein.

Depreciation Expense

At the end of the test period, Windsor had recorded depreciation expense of \$886. The Commission, in its disallowance of a capital item of \$4,106 included in the cost of maintaining the treatment and disposal plant as discussed earlier, has allowed a pro forma depreciation expense adjustment of \$1,369 computed on the basis of a 3-year service life of the property more appropriately included in Account No. 373, Treatment and Disposal Equipment. Therefore, the Commission's reasonable adjusted depreciation expense for the test period is \$2,255⁶ for rate-making purposes.

Amortization Expense

The Commission, pursuant to its examination of invoices contained in the cost of maintaining the treatment and disposal

⁶ Depreciation Expense, per books at 12/31/83	\$ 886
Add: Depreciation expense on capital item transferred from maintenance of treatment plant - \$4,106 X 33.33 percent	1,369
Total allowable depreciation expense	<u>\$2,255</u>

system, found that Windsor incurred several items of expense as explained above, which were classified as being non-recurring in nature. The Commission is of the opinion that Windsor should be allowed to amortize these non-recurring costs over a 3-year period and has included \$389⁷ in test year expense.

Property Taxes

The Commission has reduced Windsor's property taxes for the test period of \$1,061 by \$607. Windsor erroneously included in test period property tax expense payments applicable to 1982 taxes pertaining to the Kentucky Department of Revenue of \$602, and a payment of \$5 to the Secretary of State - Kentucky.

Other Interest Expense

Windsor reported test-period interest expense of \$3,462 on debt to Carroll Cogan Companies Special Loan Account. The Commission takes judicial notice that this amount represents interest expense on a loan from the Carroll Cogan Companies Special Loan Account.⁸ A review of Windsor's annual reports indicates that this loan is actually a note payable of \$29,088 which was entered into in 1982. The Commission notes that Windsor failed to supply a copy of this indebtedness with its application and that Windsor never requested nor was it granted approval to enter into this indebtedness. Furthermore, the Commission notes from other instances in which the Carroll Cogan Companies Special

⁷ \$1,166 X 33.33% = \$389.

⁸ Refer to Order in Case No. 9101, The Application of Enviro Utilities, Inc., For an Adjustment of Rates Pursuant to the Alternative Rate Filing Procedure for Small Utilities.

Loan Account loaned money to associated sewer utilities that such loans were taken out to pay current obligations and, thus, the allowance of this interest expense would constitute retroactive rate-making. Moreover, because Windsor neither requested nor was granted approval to enter into this indebtedness, the Commission has disallowed this interest expense of \$3,462 for rate-making purposes.

Income Taxes

Windsor projected pro forma federal and state corporate income taxes, and Jefferson County 2.2 percent Occupational Tax totalling \$2,410 for the test period. The Commission is of the opinion that the federal and state corporate income taxes, and the Jefferson County 2.2 percent Occupational Tax should be allowed for rate-making purposes and the computation will be made in a later section of this Order.

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

	<u>Windsor Adjusted</u>	<u>Commission Adjustments</u>	<u>Commission Adjusted</u>
Operating Revenues	\$ 37,275	\$	\$ 37,275
Operating Expenses	57,122	<11,237>	45,885
Net Operating Income	<u>\$<19,847></u>	<u>11,237</u>	<u>\$ <8,610></u>
Interest Expense	3,474	<3,462>	12
<u>Net Income</u>	<u>\$<23,321></u>	<u>\$ 14,699</u>	<u>\$ <8,622></u>

REVENUE REQUIREMENTS

The Commission is of the opinion that Windsor'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 Windsor to meet its operating expenses, service its debt and provide a reasonable return to its stockholders. Therefore, the Commission finds that Windsor should be permitted to increase its rates to produce total annual revenues of \$53,918,⁹ which includes federal, state and Jefferson County income tax expenses of \$1,553 and interest expense of \$12. This results in an annual increase in revenue to Windsor of \$16,643.

SUMMARY

On January 14, 1985, Windsor submitted notice to the Commission of its intent to begin charging the rates advertised in its original application as of February 15, 1985. In a letter of the Commission dated February 11, 1985, the effective date was recognized to be March 6, 1985. In its Order of February 28, 1985, the Commission ordered Windsor to maintain its records in such manner as would enable it, or the Commission, or any of its customers, to determine the amounts to be refunded and to whom due in the event a refund is ordered upon final determination of this case in accordance with 807 KAR 5:076, Section 8.

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

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

⁹ $\langle \$45,885 + \$1,553 \rangle \div 88\% = \$53,906 + \$12 = \$53,918.$

2. The rates charged by Windsor on and after March 6, 1985, are in excess of the rates approved herein, and therefore, the difference should be refunded to the appropriate customers.

3. The rates in Appendix A are the fair, just and reasonable rates to charge for sewage services rendered to Windsor's customers and should produce annual revenues of approximately \$53,918.

IT IS THEREFORE ORDERED that the rates in Appendix A be and they hereby are the fair, just and reasonable rates of Windsor for sewage services rendered on and after the date of this Order.

IT IS FURTHER ORDERED that the rates proposed by Windsor be and they hereby are denied.

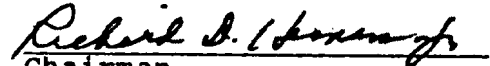
IT IS FURTHER ORDERED that the revenues collected by Windsor subsequent to March 6, 1985, through rates in excess of those found reasonable herein shall be refunded in the first billing after the date of this Order.

IT IS FURTHER ORDERED that Windsor shall file a statement within 30 days of the date of this Order reflecting the number of customers billed, the amount collected under the rates put into effect on March 6, 1985, the number of customers receiving a refund, the amount refunded and the date of the refund.

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

Done at Frankfort, Kentucky, this 26th day of March, 1985.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE
COMMISSION IN CASE NO. 9138 DATED 3/26/85

The following rates are prescribed for the customers in the area served by Windsor Facilities, Inc., d/b/a Windsor Forest Sewer System located in Jefferson County, Kentucky. 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.

RATES: Monthly

Single Family Residential	\$7.40
Multi-Family	5.90