

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

THE APPLICATION OF ALBANY GAS UTILITY )  
COMPANY, OF CLINTON COUNTY, KENTUCKY, )  
FOR (1) A CERTIFICATION OF PUBLIC )  
CONVENIENCE AND NECESSITY TO CONSTRUCT )  
AND OPERATE A NEW NATURAL GAS DISTRI- )  
BUTION SYSTEM AT ALBANY, KENTUCKY, ) CASE NO. 9329  
(2) APPROVAL OF THE PROPOSED PLAN )  
OF FINANCING OF SAID PROJECT AND )  
(3) APPROVAL OF PROPOSED GAS RATES )  
TO BE CHARGED BY THE COMPANY TO THE )  
NATURAL GAS CUSTOMER )

O R D E R

On October 24, 1985, Albany Gas Utility Company ("Albany") filed a petition for rehearing on nine issues addressed in the Commission's Final Order of October 4, 1985. Albany requested rehearing on the issues of purchased gas expense, president/general manager's salaries, an additional field person, outside services expense, income taxes, depreciation rates, rate of return on rate base, cost of insurance and cash working capital allowance. The following is an issue-by-issue discussion of the points which were raised in Albany's application for rehearing.

Gas Purchases

Albany requested rehearing on the cost of gas the Commission used to determine the rates and charges. The Commission, in its final Order, stated that "Based on the current contract price per Mcf of gas, the current finder's fee, the projected normalized Mcf volume of sales (104,525 Mcf), the

Commission has determined annual normalized gas-purchased cost to be \$204,869. Any rate relief Albany requires as a result of escalating gas costs can be granted pursuant to the provisions of a purchase gas adjustment clause."<sup>1</sup> The Commission used the only contract price available at the time of the Order and advised Albany of the method to use with regard to increases or decreases to the average cost of gas. At the hearing, Albany was informed by the Hearing Officer that its tariff should be filed containing its rules and regulations, including a purchase gas adjustment clause.<sup>2</sup> The mechanism is available to Albany to procure rate relief for purchased gas cost increases, therefore, rehearing on this issue is hereby denied.

President/General Manager's Salary

Albany submitted that its president/general manager should be paid \$40,000 annually instead of the \$30,000 allowed by the Commission, citing Albany's uniqueness in having numerous sources of supply and the necessity of marketing Albany to new customers. At the time of the original submission of this case, Albany had one contracted supplier and, as of the filing of the petition for rehearing, Albany cites only the expectations of some 40 additional suppliers whose reserves and ability to deliver are equally speculative.

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<sup>1</sup> Commission Order dated October 4, 1985, p. 4.

<sup>2</sup> Hearing Transcript, July 16, 1985, pp. 34-35; Questions 76-78.

The marketing of natural gas to new customers is inherent in new gas systems. The Commission, however, believes that the marketability is based more on price, deliverability and reliability rather than sophisticated advertising or promotional campaigns to persuade potential customers.

Furthermore, the cost burden of providing price-effective, reliable delivered natural gas is fully provided for in the cost components of the rate structure. The Commission has allowed a finder's fee of 16 cents per Mcf, full cost recovery of cost of purchased gas, salaries of \$40,000 to \$46,000 for each of the three principals capitalized to rate base during the 5-year proposed construction, and the Albany-proposed cost of capital of 10 percent, which compares favorably to cost of capital provided to systems of a similar size. Thus, the entrepreneurial skills necessary for the general manager were fully considered and compensated and the Commission denies rehearing on this issue.

#### Additional Field Personnel

Citing that the expected number of suppliers will approach 40, Albany believes that one additional field person is necessary to assure an uninterrupted supply of natural gas.

As stated, at the time of the final Order in this case, Albany had one committed supplier and, at the time of the filing of the application for rehearing, Albany stated that it has "several" verbal commitments which are expected to be reduced to writing in the next few weeks.

Without having had the opportunity to scrutinize the necessity for and the reliability of some 40 prospective suppliers

(one supplier for every 13 projected customers), the Commission believes that consideration of additional field personnel wage expense is highly speculative as a practical matter. Secondly, the Commission allowed a field person's salary of \$18,000 and part-time labor of \$6,000 to be expensed on an on-going basis while also allowing the capitalization of approximately \$113,775 in field personnel salaries during the construction period. Consequently, the Commission has provided for more than the two field personnel requested through the construction period which lasts through 1989. Therefore, the Commission denies rehearing on this issue.

#### Outside Services

Albany stated in its petition for rehearing that its outside services should be increased to \$8,000 annually, at least initially, in order to give the utility some breathing room.

In the original evidence of record, Albany sought no monies for outside services. In determining a reasonable cost of service for Albany, the Commission found that it was unreasonable and unfair to expect Albany not to incur outside services expense on an on-going basis. Therefore, the Commission allocated \$2,400 annually to this account, as it is the typical expenditure for outside services for a utility of Albany's size. In its application for rehearing, Albany offered no new evidence which the Commission had not previously considered. Therefore, rehearing is denied on this issue.

### Income Tax Expense

Albany requested in its rehearing application that the Commission grant Albany income tax expense regardless of Albany's "Sub Chapter S" tax status.

The return on rate base used by the Commission is intended to produce a pre-tax rate of return on invested capital to the corporate investors. Albany may have well been aware of this fact as it did not consider income tax expense, investment tax credits, or deferred tax credits in its calculation of cost of service and its calculation of rate base. Regardless, the Commission's intent to not allow income tax on a sub Chapter S corporation was clear and the Commission's formulation of its intent is well known and is an established practice. Therefore, the Commission denies rehearing on this issue.

### Depreciation Expense

Based on the 20-year term of its franchise with the City of Albany, Albany sought reconsideration of the depreciation rates approved by the Commission. Albany submitted that the franchise is for only 20 years and is a risk which, at the very least, should result in a compromise position with respect to useful life of the system.

The Commission is of the opinion that nonrenewal of the franchise is not known nor measurable and, in fact, the probability of nonrenewal of the franchise is remote. Additionally, given the fact that the system can be resold, thus utilizing the system's remaining useful life, the potential economic

impairment is further reduced. Therefore, the Commission denies rehearing on this issue.

#### Rate of Return on Rate Base

In its rehearing application, Albany sought a rate of return on rate base of 18 percent. Albany cited that additional risk associated with potential gas supply failures entitle it to the additional return.

In its original filing in this case, Albany requested and the Commission approved a 10 percent rate of return on rate base as the return was comparable, when considering Albany's additional risk, to those rates of return granted other gas utilities of a similar size. Since the return on rate base is above those currently being granted to similar sized utilities to allow consideration of Albany's additional risk, and, since the rate of return on rate base granted was the return Albany requested, the Commission denies rehearing on this issue.

#### Insurance Expense

In its original application, Albany proposed and the Commission accepted \$12,500 in annual insurance expenses. In its rehearing application, Albany stated that, in fact, insurance cost will be approximately \$24,000 annually. Albany provided no documentation to support this assertion.

The Commission is of the opinion that the difficulty of estimating expected expenses in initial construction, finance and rate cases results in some estimates that will be high, others low; however, the total cost of service will be roughly approximated. To consider the increase in an isolated item of

expense while ignoring the likelihood of decreases in the estimation of other expenses is neither fair nor reasonable. Expense estimates reflect the best information and best application of that information at a specific point in time. Moreover, to continuously update costs as they change or become known would make it virtually impossible to complete a rate case. Therefore, the Commission denies rehearing on this issue.

#### Working Capital

Albany objected to the Commission's allowance of \$16,236 in cash working capital and suggested that the allowance may not comport with applicable Commission practices or policies. Albany did not state how it thought working capital should be determined, nor did it state what practices or policies to which the allowance did not comport.

However, the Commission did review its working papers regarding Albany's cash working capital allowance and has found that the cash working capital allowance should be \$16,233. Since the \$3 difference is de minimis, the Commission denies rehearing on this issue.

#### FINDINGS AND ORDERS

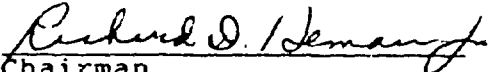
The Commission, after consideration of the evidence of record and being advised, is of the opinion and finds that:

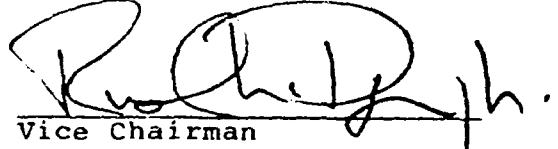
1. The petition for rehearing contained no evidence which was not considered in the Commission's final Order.

IT IS THEREFORE ORDERED that the petition for rehearing of October 24, 1985, is hereby denied and the Commission's Order entered October 4, 1985, is hereby affirmed.

Done at Frankfort, Kentucky, this 13th day of November, 1985.

PUBLIC SERVICE COMMISSION

  
Chairman

  
Vice Chairman

  
Commissioner

ATTEST:

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Secretary