

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF FERN HILL UTILITIES,)	
INC., FOR AN ADJUSTMENT OF RATES PURSUANT)	
TO THE ALTERNATIVE RATE ADJUSTMENT FOR)	CASE NO. 9102
SMALL UTILITIES)	

O R D E R

On March 20, 1985, the Commission issued a final Order in this case finding that Fern Hill Utilities, Inc., ("Fern Hill") had sufficient revenues. This Order also finds a revenue sufficiency and, therefore, does not grant additional revenues.

On April 8, 1985, Fern Hill filed a petition for rehearing of three issues: routine maintenance expense, original cost of utility plant, and interest expense on long-term debt. The Commission's Order of April 29, 1985, granted rehearing on these issues. Rehearing of the routine maintenance expense issue was held on June 5, 1986, in a companion case, Case No. 9101, The Application of Enviro Utilities, Inc., For an Adjustment of Rates Pursuant to the Alternative Rate Filing Procedure for Small Utilities. The remaining two issues were scheduled for rehearing on June 25, 1985. On June 14, 1985, Fern Hill requested a postponement of the June 25 hearing to the period of July 15 through July 20, 1985. On June 18, 1985, Fern Hill's rehearing was continued until further notice.

By correspondence of July 23, 1985, the Commission required Fern Hill to mail a notice statement of the proposed rates to each of Fern Hill's customers. By its Order of October 2, 1985, the Commission scheduled rehearing for October 15, 1985, on the remaining issues of original cost of utility plant and interest expense on long-term debt. During the rehearing several of Fern Hill's customers presented testimony and comments concerning the reasonableness of Fern Hill's proposed rates. Fern Hill offered no testimony, no comments, and presented no exhibits.

On November 6, 1985, Fern Hill filed a brief wherein it stated that it declined to pursue any further the issues of original cost of utility plant-in-service or interest expense on long-term debt at this time.

The following discusses the Commission's findings and opinions regarding the issues of: routine maintenance expense, original cost of utility plant-in-service, and interest expense on long-term debt.

Routine Maintenance Expense

As understood, the Commission's determination with respect to the routine maintenance issue in Case No. 9101 will be followed in this case. Therefore, the findings with regard to the routine maintenance fee as delineated in the Order in this proceeding dated March 20, 1985, are affirmed. Thus, no increase in the routine maintenance fees is allowed.

Original Cost of Utility Plant-in-Service

The Commission's initial finding and conclusion in this case was that Fern Hill's utility plant-in-service was fully

contributed, fully recovered through the sale of lots or fully depreciated except for plant additions of \$14,439 since the acquisition of Fern Hill. Having been presented with no evidence contrary to its original determination, the Commission affirms its original conclusion on this issue.

Interest Expense on Long-Term Debt

In its original decision, the Commission denied depreciation expense and the amortization expense on the plant acquisition adjustment. In similar instances the Commission would not allow the interest expense on debt to finance the acquisition of the plant. However, in this case the circumstances are somewhat unique and the Commission gave further consideration to the interest expense issue. First, upon the acquisition of Fern Hill by Carroll Cogan Companies, Inc. ("CCC"), the mortgage was reissued at the amount outstanding at the time of the transfer plus amounts for certain prior period operating losses which were disallowed for rate-making purposes in the Case No. 7803.¹ The prior mortgage had been legally secured by an exclusive pledge of the assets of Fern Hill and in full force of legal fact was an obligation to Fern Hill. Therefore, the lien on the sewer property was valid and consequently became an obligation of the sewer utility. Second, the Commission allowed, in Case No. 7803, the

¹ Application of Andriot-Davidson's Service Co., Inc., D/B/A Fern Hill Utility, Inc., for Authority to Acquire and Operate the Sewage Treatment Plant Operated by Fern Hill Co., Inc., in Jefferson County, Kentucky and Application of Andriot-Davidson's Service Co., Inc., D/B/A Fern Hill Utility, Inc., for an Order Adjusting the Rates Currently Charged by Fern Hill Co., Inc.

purchase of Fern Hill by CCC and included interest on the long-term debt in determining the revenue requirements of Fern Hill under the new ownership. Third, the payment of principal and interest on the outstanding debt of Fern Hill requires a cash outlay which cannot be met without some provision for interest expense for rate-making purposes. Therefore, in the interest of fairness to the utility and as a measure of security for the continued safe and reliable operation of Fern Hill for the benefit of the ratepayers the Commission included a provision for interest on long-term debt for rate-making purposes in this instance. As a means of minimizing the impact of this cost to the ratepayers and to spread the financing cost to the ratepayers equally over the life of the loan, the Commission continued the methodology established in Fern Hill's last case of using the average interest expense over the life of the loan. Therefore, in consideration of the realities of Fern Hill's unique situation, and upon a thorough review of the reasonableness of the rates granted herein, the Commission concluded that \$21,239 is the appropriate annual interest expense to be used for rate-making purposes in this instance.

Since Fern Hill declined to pursue this issue on rehearing through its brief of November 6, 1985, and has offered no new evidence which could be subject to review by the Commission or the intervenors, the Commission must affirm its original decision.

However, Fern Hill did offer an objection to the fairness of the Commission's decision to use the average interest expense over the life of the loan. In summary, Fern Hill cited that the near term cash shortfall due to this decision is approximately \$12,000

annually with no assurance of further recovery due to potential acquisition of Fern Hill by Louisville and Jefferson County Metropolitan Sewer District ("MSD"). The Commission considers the substance of this objection to be highly speculative in that it attempts to predict the outcome of economic events subject to negotiation and is based on some unspecified future time period. Furthermore, the Commission believes in this case that Fern Hill was treated very fairly in regard to the rate-making treatment of interest expense on long-term debt. The Commission is of the opinion if Fern Hill is concerned about losing any investment in its operations through the acquisition of Fern Hill by MSD, that Fern Hill should negotiate for its economic interests with that agency if and when the acquisition occurs.


SUMMARY

The Commission, after consideration of the evidence of record and being advised, is of the opinion and finds that its original Order of March 20, 1985, should be affirmed in its entirety.

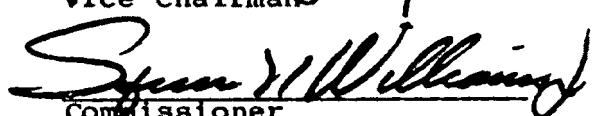
IT IS THEREFORE ORDERED that the Commission's Order of March 20, 1985, is affirmed in its entirety.

Done at Frankfort, Kentucky, this 3rd day of September, 1986.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Executive Director