COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF NEWMARKET, INC., FOR AN ADJUSTMENT OF RATES PURSUANT TO THE ALTERNATIVE PROCEDURE FOR SMALL UTILITIES	)	CASE NO. 9676

O R D E R

IT IS ORDERED that:

1. The Staff Report for Newmarket, Inc., attached hereto as Appendix A shall be included as a part of the record in this proceeding. In the event a public hearing is held, Staff preparing the Staff Report will be available for cross-examination.

2. Newmarket shall have until the close of business December 16, 1986, to file written comments concerning the contents of Appendix A. In the event Newmarket desires a public hearing, it shall file a Motion requesting such hearing, with a copy to all parties to record.

Done at Frankfort, Kentucky, this 2nd day of December, 1986.

PUBLIC SERVICE COMMISSION

For the Commission

ATTEST:

Executive Director

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

STAFF REPORT

ON

NEWMARKET, INC.

CASE NO. 9676

Prepared By: Mark Frost
Public Utilities Financial
Analyst, Senior
Water and Sewer Revenue
Requirements Branch
Rates and Tariffs Division

Prepared By: Jordan Neel
Public Utilities Rate
Analyst, Principal
Communication, Water and
Sewer Rate Design Branch
Rates and Tariffs Division

APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE COMMISSION
IN CASE NO. 9676 DATED 12/02/86

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

STAFF REPORT

ON

NEWMARKET, INC.

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STAFF REPORT

ON

NEWMARKET, INC.

CASE NO. 9676

PREFACE

On August 27, 1986, Newmarket, Inc., ("Newmarket") filed its application seeking to increase its rate pursuant to the Alternative Rate Filing Procedure for Small Utilities. The proposed rate would generate approximately $13,302 on an annual basis, an increase of approximately 50 percent in the rate currently being charged.

As part of its endeavor to shorten and simplify the regulatory process for utilities the Commission chose to perform a limited financial review of Newmarket's operations for the test year, calendar year 1985. The Commission's objective was to substantially reduce the need for written data requests, decrease the time necessary to examine the application and, therefore, decrease the expense to the utility. Mark Frost and Jordan Neel of the Commission's Division of Rates and Tariffs performed the review on October 22, 1986, at the office of Newmarket in Louisville, Kentucky.

SCOPE

The scope of the review was limited to obtaining information to determine whether the test year operating expenses as reported in Newmarket's 1985 Annual Report were representative of normal operations and to gather information to evaluate pro forma

adjustments proposed in Newmarket's filing. Expenditures charged to test year operations were reviewed as were the invoices. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

FINDINGS

Billing Analysis and Normalized Revenue

Newmarket has proposed to decrease the number of customers from 146 to 144 and has adjusted annual revenue by a $362 loss due to fewer customers. In conference with the owner-manager it was found that the loss of two customers was based on the average of vacancy time within the entire system for one year. All such vacancies are expected to be filled at a future date with no permanent disconnections anticipated. The adjustment in revenue of $362 was based on the estimated vacancy time.

During the conference it was found that the owner-manager continues to receive sewer service at no charge. As Newmarket's tariff makes no provision for providing free service to any of its customers, an increase in test-year revenues to reflect the elimination of the effect of providing free service to the owner-manager should be made.

The number of customers should be adjusted to 147, disallowing the proposed customer count of 144 and increasing that count by one residential customer to include the owner-manager.

Annualized revenue for Newmarket should be based on 136 residential customers at a rate of 14.80 per month, and 11 commercial customers classified at a total usage level of 53 residential equivalents at a rate of $22.60 per residential

equivalents per month. The annualized revenue for Newmarket is $38,527.

Maintenance Expense

Newmarket proposed a pro forma level of maintenance expense of $13,741, an increase of $7,620 over the actual test period level. The pro forma adjustment was based on the age of the plant causing more frequent repairs than prior years. The only supporting evidence provided at the field review were the invoices for 1986. Staff reviewed the invoices and concluded that the majority of them were capital expenditures. Staff also discovered that the actual test period level included the cost of the installation of a new blower which is considered a capital expenditure. Staff recommends that maintenance expense be reduced by $11,160 to reflect the disallowance of the proposed adjustment and test period capital expenditure, for an adjusted level of $2,581. Depreciation expense on the aforementioned capital expenditures will be discussed in a latter section.

Professional Fees

Newmarket proposed a pro forma level of professional fee expense of $1,000, the cost of filing the rate case. Since the filing of a rate case is not considered a normal yearly occurrence it is normal practice to amortize the cost over a 3-year period. Therefore, staff recommends amortizing the cost of the rate case over 3 years for a reduction of $667.

Depreciation Expense

Newmarket does not record depreciation expense due to the entire cost of the plant being recovered through the sale of lots.

As discussed in a previous section, Newmarket has made several capital expenditures either during 1986 or the test period. After reviewing the invoices, staff has calculated the following depreciation schedule:

Invoice Date	Description	Invoice Amount	Depreciation Life	Depreciation Expense
6/14/85	Installation New Blower per Jefferson County Health Dept.	$ 3,540	7	506
2/13/86	Installed New Sludge Return Blower per Jefferson County Health Dept.	1,035	7	148
4/9/86	Installed New 1-1/2" Water Service	1,885	20	94
5/23/86	Installed Out of Service D/Unit Blower on Surge Tank & Replaced Diffussors per Health Dept. and Owners	1,050	7	150
6/12/86	Replaced Defective Air Drops & Diffussors in Digestor Tank per Health Dept. & PSC	928	7	133
6/12/86	Repairs to Air Drops in Double Unit Aeration Tank	690	7	99
8/1/86	Repairs to Main Sewer Between 2402 & 2404 Baylor Drive	1,671	20	84
8/1/86	Installed Dual Auto. Switch Over Chlorination Equipment per PSC Report	2,124	7	303
8/27/86	Installed 6' Sewer Service & Tap Main	2,030	20	102
	TOTAL	$14,954		1,618

It is staff's opinion that items purchased in 1986 are outside the actual test period, however, the depreciation expense associated with these items would be an ongoing or future expense. Therefore, staff recommends that depreciation expense of $1,618 be included in operating expenses for the test period.

Outside Services

Newmarket reported outside services expense of $2,350 for the test period. At the field review, staff noted that Newmarket included a $450 payment to the WWT Council Legal Fund. This payment was for the legal representation of the owners in negotiations with the Metropolitan Sewer Board. Staff is of the opinion that this benefits the owners only and has no direct benefit to the ratepayers. Therefore, staff recommends that outside services be reduced by $450 for an adjusted level of $1,900.

Other Expenses

Upon review of Newmarket's financial records, staff noted that Newmarket correctly excluded expenses from December, 1984, but also neglected to include expenses incurred during December, 1985, but paid January, 1986. Therefore, test period expenses are for an 11-month rather than a full 12-month period. The excluded expenses are as follows:

Invoice Date	Description	Date Paid	Amount
12/4/85	Sludge Hauling	1/27/86	$ 825
	Cleaning Chlorine Tank		298
12/20/85	Sludge Hauling	2/28/86	300
	KPDES Lab Change		204
	Chlorine Gas		242

Therefore, staff recommends that test period operating expenses be increased by $1,869 to reflect a full 12-month expense level.

SUMMARY

Based on the recommendation proposed by Staff in this report, Newmarket's operations are as follows:

	Newmarket Pro Forma	Recommended Adjustments	Staff Pro Forma
Operating Revenues	$ 35,567	$ 2,960	$38,527
Operationg Revenues	50,171	<8,786>	41,385
Net Operating Income	$<14,609>	$11,746	$<2,858>

REVENUE REQUIREMENTS

The staff's proposed pro forma operations provide Newmarket an operating ratio of 107.4 percent. Staff is of the opinion that a ratio of 88 percent is a fair, just and reasonable operating ratio in that it will enable Newmarket to pay its operating expenses and provide a reasonable return to its owner. Therefore, staff recommends that Newmarket be granted an increase of $8,502.

Dividends

Staff noted, during the field review, that Newmarket paid approximately $3,000 in dividends during the test period. The dividends paid during the period are questionable considering the financial condition of Newmarket. Staff recommends that in the

future Newmarket should review its financial records to determine if the utility is capable to pay dividends without deteriorating its financial position rather than paying dividends on a routine basis.

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