

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF J&W SANITATION)	
COMPANY FOR A RATE ADJUSTMENT PURSUANT)	CASE NO. 92-322
TO THE ALTERNATIVE RATE FILING)	
PROCEDURE FOR SMALL UTILITIES)	

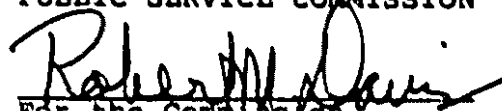
O R D E R

On August 7, 1992, J&W Sanitation Company ("J&W") filed its application for Commission approval of a proposed increase in its rates for sewer service. Commission Staff, having performed a limited financial review of J&W's operations, has prepared the attached Staff Report containing Staff's findings and recommendations regarding J&W's proposed rates. All parties should review the report carefully and provide any written comments or requests for a hearing or informal conference no later than 15 days from the date of this Order.

IT IS THEREFORE ORDERED that all parties shall have 15 days from the date of this Order to provide written comments regarding the attached Staff Report or requests for a hearing or informal conference. If no request for a hearing or informal conference is received, then this case will be submitted to the Commission for a decision.

Done at Frankfort, Kentucky this 2nd day of November, 1992.

PUBLIC SERVICE COMMISSION


For the Commission

ATTEST:



Executive Director

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STAFF REPORT

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Requirements Branch
Rates and Tariffs Division

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Analyst
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STAFF REPORT
ON
J&W SANITATION COMPANY
CASE NO. 92-322

A. Preface

On August 7, 1992, J&W Sanitation Company ("J&W") filed an application with the Commission seeking to increase its sewer rate pursuant to the Alternative Rate Filing Procedure for Small Utilities. The proposed rate would generate approximately \$5,712 annually in additional revenues, an increase of 68 percent over normalized test-year revenues of \$8,400.

In order to evaluate the requested increase, the Commission Staff ("Staff") chose to perform a limited financial review of J&W's operations for the test period, calendar year 1991. At J&W's request, Carl Salyer Combs of the Commission's Division of Rates and Tariffs assisted J&W with the preparation of its application and conducted the review at the home of Clyde Fowler, J&W's owner, in Madisonville, Kentucky on July 28, 1992 and is responsible for this Staff Report except for the sections on operating revenues and rate design which were prepared by Nicky Moore of the Commission's Research Division. During the course of the review, J&W was advised that all proposed adjustments to test-year expenses must be supported by some form of documentation, such as an invoice, or that all such adjustments must be known and measurable. Based upon

the findings of this report, Staff recommends that J&W be authorized to increase its annual operating revenues by \$5,119.

Scope

The scope of the review was limited to obtaining information to determine whether reported test-period operating revenues and expenses were representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

B. Analysis of Operating Revenues and Expenses

Operating Revenues

In its application, J&W reported test-year revenue of \$8,615. Its application also indicates that, at the time of the filing, it had 68 customers, but pursuant to a subsequent telephone discussion, J&W disclosed that it is serving, and was serving at the end of the test year, 70 customers. This number of customers would generate \$8,400¹ in revenue annually at current rates. Therefore, for the purpose of this report, the staff will use \$8,400 as the adjusted revenue for ratemaking purposes.

Operating and Maintenance Expenses

J&W reported test-period operating expenses of \$4,679 which it proposed to increase by \$9,451. Staff's adjustments to test-period operations are discussed in the following sections:

¹ Flat Rate of \$10.00 per month x 70 customers x 12 months = \$8,400.

Management Fee

J&W reported no test-year payments for management services, but has proposed an annual management fee of \$2,400. The Commission's past practice has been to allow a management fee for small sewer utilities. In this instance, Staff is of the opinion that J&W is entitled to an annual management fee and that \$2,400 is a reasonable level. Therefore, Staff recommends inclusion of an annual management fee of \$2,400 for rate-making purposes.

Chemicals

J&W reported no test-year chemicals expense, but proposed an annual expense of \$625. In support of its proposed adjustment, J&W provided a quotation from PB&S Chemical Company which shows that a 53-gallon drum of sodium hypochlorite costs \$125. Mr. Fowler, J&W's owner, opined that the treatment plant requires 5 drums annually. Staff reviewed reported 1991 chemicals expense of 5 similar-sized sewer utilities (with regard to number of customers) and found those 5 to have an average annual chemicals expense of \$611. Also, the Commission's Engineering Division considers the proposed adjustment to be reasonable. Therefore, Staff recommends that annual chemicals expense of \$625 be included for rate-making purposes.

Maintenance of Treatment and Disposal Plant

J&W proposed to increase reported test-year maintenance of treatment and disposal plant expense of \$779 by \$315 based upon the purchase in 1992 of a pump and a motor for which invoices were

provided. Staff recommends that these two items be capitalized and depreciated over an appropriate period. This matter will be addressed further in a section on depreciation expense and Staff recommends inclusion of annual maintenance of treatment and disposal plant expense of \$779 for rate-making purposes.

Customer Records and Collection Expense

J&W proposed to increase reported test-year customer records and collection expense of \$174 by \$3,066 based upon a quote from Dorn Fowler of \$270 per month to provide various bookkeeping and billing services. In past cases involving small sewer utilities, the Commission has allowed an annual expense of \$1,200 and Staff is of the opinion that annual customer records and collection expense of \$1,200 is reasonable. Since J&W's customers are charged a flat rate, no calculations are involved in the preparation of customers' bills. Dorn Fowler's quote includes "bookkeeping services required to prepare monthly operating reports." In Staff's opinion, sewer utilities with as few as 68 customers do not usually prepare monthly operating statements. With so small a customer base, the cost of preparing monthly operating reports would outweigh the benefit to the customers. Staff recommends annual customer records and collection expense of \$1,200 and that amount has been included for rate-making purposes.

Office Supplies and Other Expense

J&W proposed to increase reported test-year office supplies and other expense of \$121 by \$179 to more correctly reflect the

normal annual expense. Staff has calculated the annual expense for stamps and envelopes needed to mail 68 customer bills monthly to be approximately \$245². J&W also needs additional stamps and envelopes to mail payments to a handful of vendors and other office supplies such as ledger sheets, staples, paper clips, pencils, etc. Staff is of the opinion that an annual office supplies and other expense of \$300 is reasonable and recommends that amount be included for rate-making purposes.

Insurance Expense

J&W proposed to increase reported test-year insurance expense of \$644 by \$1,094 based upon an increase in the cost of liability insurance on the sewage treatment plant and inclusion of the cost to insure a 1983 Chevrolet pick-up truck which Mr. Fowler drives to and from the treatment plant. In support of its proposed adjustment, J&W provided copies of quotes from insurance agents which totalled \$1,689. Since the proposed adjustment is known and measurable, Staff recommends that it be accepted and annual insurance expense of \$1,689 has been included for rate-making purposes.

² 68 bills X \$.29 postage = \$19.72 per month
\$19.72 X 12 months = \$236.64

68 envelopes per month X 12 months =
816 envelopes annually; at a cost of approximately \$1 per
hundred, the annual cost for envelopes would be approximately
\$8.

\$237 + \$8 = \$245

Regulatory Commission Expense

J&W reported no test-year regulatory commission expense, but proposed to include the cost of quarterly sampling and analysis to satisfy the minimum requirement of the Division of Water of the Kentucky Department for Environmental Protection. In support of its proposed adjustment, J&W provided a copy of a quotation from McCoy & McCoy Laboratories, Inc. which reflects a quarterly charge of \$76. Therefore, Staff recommends inclusion of annual regulatory commission expense of \$304 related to testing fees for rate-making purposes.

J&W did not include the \$650 cost of its required Kentucky Pollutant Discharge Elimination System permit. Since the permit covers a period of 5 years, Staff recommends that a prorated annual expense of \$130 be included for rate-making purposes. Together with the aforementioned recommendation of \$304 related to testing fees, Staff recommends total annual regulatory commission expense of \$434 for rate-making purposes.

Transportation Expense

J&W proposed to increase reported test-year transportation expense of \$12 by \$988 to more correctly reflect an adequate annual expense. Mr. Fowler asserts that he travels to the treatment plant a minimum of six days per week and that a round-trip visit consumes about 12 miles. At that rate, Mr. Fowler would log approximately

3,744³ miles annually. At the allowable rate for federal income tax purposes of 28 cents per mile, J&W's annual expense would be \$1,048. Therefore, Staff recommends inclusion of annual transportation expense of \$1,048⁴ for rate-making purposes.

Rent Expense

J&W reported no test-year rent expense, but proposed an annual expense of \$360 to cover the cost of an office for the utility and a telephone to receive calls from its customers. Staff is of the opinion that Mr. Fowler is entitled to compensation for maintaining an office in his home and that \$30 per month is a reasonable amount. Therefore, Staff recommends that annual rent expense of \$360 be included for rate-making purposes.

Depreciation Expense

J&W reported test-year depreciation expense of \$227 and proposed no adjustment to that amount. As mentioned previously in the section on maintenance of treatment and disposal plant, J&W proposed an increase to that expense based upon the purchase of a pump and motor at a total cost of \$315. According to the Commission's Engineering Division, five years is an appropriate period over which to depreciate both the pump and the motor. Since Staff recommends that these two items be capitalized and

³ 12 miles per trip x 6 days per week = 72 miles weekly x 52 weeks = 3,744 miles annually.

⁴ 3,744 x \$0.28 = \$1,048

depreciated, annual depreciation expense of \$63⁵ related to those items has been included for rate-making purposes. Combined with the aforementioned reported test-year depreciation expense of \$227, Staff recommends inclusion of total annual depreciation expense of \$290⁶ for rate-making purposes.

Taxes Other Than Income Tax Expense

J&W reported test-year taxes other than income tax expense of \$70 and proposed no adjustment to that amount. Since J&W did not include the annual Public Service Commission assessment of \$50, Staff recommends that that amount be included as it is known and measurable. Therefore, Staff recommends inclusion of total annual taxes other than income tax expense of \$120 for rate-making purposes.

Operations Summary

Based on the recommendations of Staff contained in this report, J&W's operating statement would appear as follows:

	<u>Test Year Actual</u>	<u>Recommended Adjustments</u>	<u>Test Year Adjusted</u>
OPERATING REVENUES:	\$ 8,615	\$< 215>	\$ 8,400
OPERATING EXPENSES:			
Management Fee	\$ -0-	\$ 2,400	\$ 2,400
Collection System Labor	75	-0-	75
Water Cost	2,313	-0-	2,313
Chemicals	-0-	625	625
Coll. System Supplies	56	-0-	56
Maint. of Coll. System	175	-0-	175
Maint. of Treatment and Disposal Plant	779	-0-	779

⁵ \$315/5 years - \$63 annually

⁶ \$227 + \$63 = \$290

Customer Records and Accounts	174	1,026	1,200
Office Supplies and Other	121	179	300
Insurance	644	1,045	1,689
Reg. Commission	-0-	434	434
Transportation	12	1,036	1,048
Miscellaneous General	33	-0-	33
Rent	-0-	360	360
Depreciation	227	63	290
Taxes Other Than Income	70	50	120
Total Operating Expense	<u>\$ 4,679</u>	<u>\$ 7,218</u>	<u>\$11,897</u>
NET INCOME	<u>\$ 3,936</u>	<u>\$ <7,433></u>	<u><3,497></u>

C. Revenue Requirements Determination

The approach frequently used by the Commission to determine revenue requirements for small, privately-owned utilities is the calculation of an operating ratio.⁷

This approach is used primarily when there is no basis for a rate-of-return determination or due to the fact that the cost of the utility plant has fully, or largely, been recovered through the receipt of contributions, either in the form of grants or donated property. The ratio generally used by the Commission in order to provide for equity growth is 88 percent. In this instance, the use of an 88 percent operating ratio applied to the test-year operating expense results in a total revenue requirement of \$13,519 and increased revenues of \$5,119.⁸ Therefore, Staff recommends an increase of \$5,119 in annual revenues.

⁷ Operating Ratio = Operating Expense/Operating Revenue.

⁸

Adjusted Operating Expense/Operating Ratio	\$11,897/.88
Revenue Requirement	13,519
Less: Adjusted Test-year Operating Revenues	<8,400>
Amount of Increase Required	<u>\$ 5,119</u>

D. Rate Design

In its application, J&W Sanitation filed a schedule of present and proposed rates and did not propose any changes in the rate structure. The Staff is in agreement that the present rate structure should not be altered. Therefore, any increase granted in the case has been added to the existing rate structure. The rates set forth in Appendix A will produce the recommended revenue requirement. The Staff recommends that those rates be approved for services rendered.

E. Signatures

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Communications, Water and
Sewer Rate Design Branch
Research Division

APPENDIX A
TO STAFF REPORT CASE NO. 92-322

The Staff recommends the following rate be prescribed for customers of utility.

<u>Customer Class</u>	<u>Rates</u>
Residential	\$16.10