

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF FARMDALE DEVELOPMENT	)	
CORPORATION FOR A RATE ADJUSTMENT	)	CASE NO. 97-456
PURSUANT TO THE ALTERNATIVE RATE FILING	)	
PROCEDURE FOR SMALL UTILITIES	)	

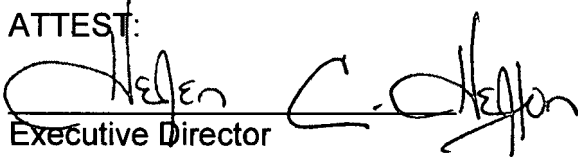
ORDER

On December 10, 1997, Farmdale Development Corporation ("Farmdale") applied for Commission approval of proposed sewer rates. Commission Staff has performed a limited financial review of Farmdale's operations and prepared the attached Staff Report containing its findings and recommendations regarding the proposed rates. All parties should carefully review the report and provide any written comments or requests for a hearing or informal conference no later than 10 days from the date of this Order.

IT IS THEREFORE ORDERED that all parties shall have no more than 10 days from the date of this Order to provide written comments regarding the attached Staff Report or to request a hearing or informal conference. If no request for a hearing or informal conference is received, this case will be submitted to the Commission for a decision.

Done at Frankfort, Kentucky, this 24th day of June, 1998.

ATTEST:

  
Executive Director

PUBLIC SERVICE COMMISSION

  
For the Commission

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STAFF REPORT

Prepared by: Beverly B. Davis  
Manager, Financial Audits Branch  
Division of Financial Analysis

Prepared by: Renee Curry  
Public Utility Rate Analyst;  
Communications, Water and  
Sewer Rate Design Branch  
Division of Financial Analysis

STAFF REPORT  
ON  
FARMDALE DEVELOPMENT CORPORATION  
CASE NO. 97-456

On December 10, 1997, Farmdale Development Corporation ("Farmdale") filed an application seeking to increase its rates pursuant to 807 KAR 5:076. To evaluate the requested increase, Commission Staff performed a limited financial review of Farmdale's test period operations; the year ended December 31, 1996.

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

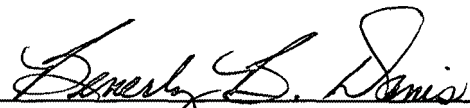
Beverly B. Davis of the Commission's Financial Audits Branch began the limited review on April 22, 1998. Ms. Davis is responsible for the preparation of this Staff Report except for the determination of normalized operating revenue and Attachment D, which were prepared by Renee Curry of the Commission's Communication, Water and Sewer Rate Design Branch.

A comparison of Farmdale's actual and pro forma operations is shown in Attachment A. Based on Staff's recommendations, Farmdale's operating statement would appear as set forth in Attachment B.

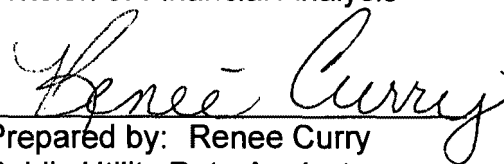
Attachment C compares Farmdale's and Staff's revenue requirement calculations. Farmdale determined its pro forma revenue requirement to be \$65,446, an increase in revenues of \$13,615. Staff recommends a revenue requirement of \$57,823

or a \$3,175 increase. The rates contained in Attachment D will achieve Staff's recommended level of revenue.

Signatures

A handwritten signature in cursive script, appearing to read "Beverly B. Davis", written over a horizontal line.

Prepared by: Beverly B. Davis  
Manager, Financial Audits Branch  
Division of Financial Analysis

A handwritten signature in cursive script, appearing to read "Renee Curry", written over a horizontal line.

Prepared by: Renee Curry  
Public Utility Rate Analyst;  
Communications, Water and  
Sewer Rate Design Branch  
Division of Financial Analysis

ATTACHMENT A  
STAFF REPORT CASE NO. 97-456  
FARMDALE'S REQUESTED OPERATIONS

	Test Year	Adjustments	Pro Forma Operations
Operating Revenue			
Flat Rate Revenue	\$ 51,831		\$ 51,831
Operating Expenses			
Management Fee	4,800	4,800	9,600
Sludge Hauling	165		165
Utility Service - Water Cost	2,869		2,869
Other - Labor	1,372		1,372
Fuel and Power	8,837		8,837
Chemicals	1,570		1,570
Routine Maintenance Fee	6,600	1,200	7,800
Maintenance of Collection System	825		825
Maintenance of Treatment Plant	1,825		1,825
Maintenance of Other Facilities	1,411		1,411
Agency Collection Fee	7,780		7,780
Office Supplies	5		5
Outside Services Employed	4,159		4,159
Insurance Expense	1,500		1,500
Regulatory Commission Expense	500		500
Transportation Expense	1,403		1,403
Miscellaneous Expense	20		20
Rents	600		600
Total Operation and Maintenance Expenses	46,241	6,000	52,241
Depreciation	1,024		1,024
Amortization		500	500
Taxes Other Than Income	661		661
Operating Expenses	47,926	6,500	54,426
Net Operating Income/(Loss)	3,905	(6,500)	(2,595)
Other Income and (Deductions)			
Interest Expense	(3,598)		(3,598)
Net Income/(Loss)	\$ 307	\$ (6,500)	\$ (6,193)

ATTACHMENT B  
STAFF REPORT CASE NO. 97-456  
STAFF'S RECOMMENDED OPERATIONS

	Test Year	Adjustments	Ref.	Pro Forma Operations
Operating Revenue				
Flat Rate Revenue	\$ 51,831	\$ 2,817	(A)	\$ 54,648
Operating Expenses				
Management Fee	4,800	(1,200)	(B)	3,600
Sludge Hauling	165			165
Utility Service - Water Cost	2,869			2,869
Other - Labor	1,372			1,372
Fuel and Power	8,837			8,837
Chemicals	1,570			1,570
Routine Maintenance Fee	6,600	900	(C)	7,500
Maintenance of Collection System	825			825
Maintenance of Treatment Plant	1,825	2,700	(D)	4,525
Maintenance of Other Facilities	1,411			1,411
Agency Collection Fee	7,780			7,780
Office Supplies	5			5
Outside Services Employed				
Bookkeeping	2,095	(492)	(E)	1,603
Accounting Fees	744	456	(E)	1,200
Other	1,320	(900)	(E)	420
Insurance Expense	1,500	(764)	(F)	736
Regulatory Commission Expense	500	(250)	(G)	250
Transportation Expense	1,403	(1,403)	(H)	-
Miscellaneous Expense	20			20
Rents	600			600
Total Operation and Maintenance Expenses	46,241	(953)		45,288
Depreciation	1,024	445	(I)	1,469
Amortization		300	(J)	300
Taxes Other Than Income	661			661
Operating Expenses	47,926	(208)		47,718
Net Operating Income	3,905	3,025		6,930
Other Income and (Deductions)				
Interest Expense	(3,598)			(3,598)
Net Income	\$ 307	\$ 3,025		\$ 3,332

ATTACHMENT B  
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STAFF'S RECOMMENDED OPERATIONS

- (A) Flat Rate Revenue. Farmdale had 248 customers with annual revenues from rates of \$51,831. Farmdale's 1997 annual report showed Farmdale had 253 customers. With 253 customers, Farmdale's annual revenue from rates should be \$54,648 ( $253 \times \$18.00 \times 12$ ). For the purposes of this report, Farmdale's 1996 normalized operating revenue will be \$54,648.
- (B) Management Fee. Farmdale's test year expenses included an owner-management fee of \$4,800. The application reported that the time to manage the plant would increase due to Division of Water ("DOW") mandates and requested an increase of \$4,800 to test year expense. Since the Commission limits this fee to \$3,600 for small investor owned utilities such as Farmdale, Staff decreased test year operations by \$1,200 and recommends that the requested increase of \$4,800 be denied.
- (C) Routine Maintenance Fee. Terry Coker provides routine maintenance for Farmdale. During the test year, his fee was \$325 per month for an annual charge of \$3,900. Test year expense for this account was \$6,600 including \$2,700 for treatment plant repairs payable to Andriot-Davidson Company ("A-D"). This was a misclassification since, according to the utility owner, A-D does not provide routine maintenance for Farmdale. The application requested \$7,800 annually for this expense citing an increase in the monthly maintenance fee due to the need to spend more time at the plant per visit and increase the number of visits per week to comply with the standards set by the DOW and the Commission. A letter from Mr. Coker dated March 5, 1998 quoted a monthly

ATTACHMENT B  
STAFF REPORT CASE NO. 97-456  
STAFF'S RECOMMENDED OPERATIONS

fee of \$625 for service and testing of the plant and lift stations four times per week. Staff allowed routine maintenance of \$7,500 (\$625 X 12) for an adjustment increasing the account by \$900.

- (D) Maintenance of Treatment Plant. Test year operations included \$1,825 for repairs to the treatment plant. Staff increased this account by \$2,700 for repair expense that was misclassified as routine maintenance fee.

- (E) Outside Services Employed.

Bookkeeping: Test year expenses included \$295 paid to Linda Wood and \$1,800 payable to Carroll Cogan, Farmdale's owner. During the review, Staff learned that Ms. Wood provided bookkeeping services for all six of Mr. Cogan's sewer utilities for \$185 per week or \$9,620 annually. Staff allocated 1/6<sup>th</sup> or \$1,603 of Ms. Wood's fee to Farmdale resulting in an increase of \$1,308 for Ms. Wood's bookkeeping services. Staff eliminated the \$1,800 expense payable to Mr. Cogan since it could not be determined that he provided any bookkeeping services. He does sign some checks, approves non-routine invoices for payment, maintains some corporate records, and arranges financing; however, these are considered management duties and are compensated by the \$3,600 management fee. The combined effect of these two changes is to reduce the amount allowed for bookkeeping services by \$492.

Accounting Fee: Test year expense included \$744 paid to the utility's certified public accountant for preparation of the Commission's annual report and state



ATTACHMENT B  
STAFF REPORT CASE NO. 97-456  
STAFF'S RECOMMENDED OPERATIONS

and federal tax returns. The fee for this service for 1998 will be \$1,200. Staff increased test year expense by \$456 to reflect this change.

Other: Test year operations included \$420 for a \$35 monthly fee paid to Smither Consulting Company for monthly inspections and reports on the condition of the Farmdale plant. The test year also included \$900 for a monthly fee of \$75 payable to Martin and Assoc. for serving as a liaison between the utility and DOW and for submission of the monthly discharge monitoring reports. Martin Cogan, son of Carroll Cogan, owns Martin and Assoc. It was reported to Staff that Martin and Assoc. does not provide this service to any sewer companies not owned by Carroll Cogan. Dealing with DOW and signing the discharge monitoring reports are part of the management function and are compensated by the management fee. Staff does not consider this a prudent, necessary expense and removed it from test year operations.

- (F) Insurance Expense. Test year expenses included \$1,500 for insurance expense. According to invoices and policies provided by the utility, the cost of a commercial package for all companies owned by Mr. Cogan was \$5,885. The policy covered 8 entities. Staff allocated the cost of the insurance equally to all entities. This results in an insurance expense of \$736 and a reduction to test year operations of \$764.
- (G) Regulatory Commission Expense. This account consists of \$500 for payment of the 1996 and 1997 treatment plant permit fees from the Franklin County Health

ATTACHMENT B  
STAFF REPORT CASE NO. 97-456  
STAFF'S RECOMMENDED OPERATIONS

Department. Test year expenses have been reduced by \$250 to limit recovery to one annual permit fee.

- (H) Transportation Expense. Farmdale's expenses included an allocation of \$1,403 for an automobile lease for Mr. Cogan. No evidence was presented regarding the amount of the lease or the method of allocation. No mileage logs or other documentation of travel was presented to justify this expense. Staff reduced test year operations by \$1,403.
- (I) Depreciation Expense. Farmdale installed a new pump at one of its lift stations in 1996 but neglected to add this item to its plant schedule. Depreciating the pump over 5 years increases depreciation expense by \$445.
- (J) Amortization Expense. Farmdale proposed an adjustment to amortize rate case expense of \$1,500 over 3 years. Rate case expenses should be amortized over the anticipated life of the rates, which usually will not exceed five years. Although Farmdale's current rates were approved almost 17 years ago, staff recommends that the amortization period be limited to 5 years for an annual rate of \$300.

ATTACHMENT C  
STAFF REPORT CASE NO. 97-456  
COMPARISON OF REQUESTED AND RECOMMENDED  
REVENUE REQUIREMENTS

	Requested by Farmdale	Proposed by Staff
Operating Expenses	\$ 54,426	\$ 47,718
Divide by: Operating Ratio	88%	88%
	<hr/>	<hr/>
Required Revenue from Operating Ratio	61,848	54,225
Add: Interest Expense	3,598	3,598
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Required Revenue	65,446	57,823
Less: Normalized Revenue	51,831	54,648
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Required Increase	\$ 13,615	\$ 3,175
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ATTACHMENT D  
STAFF REPORT CASE NO. 97-456  
RECOMMENDED SEWER RATES

RECOMMENDED RATES

Single Family Residential

\$19.05 per Month