

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF AIRVIEW ESTATES,)
INC. FOR A RATE ADJUSTMENT PURSUANT) CASE NO. 98-595
TO THE ALTERNATIVE RATE FILING FOR)
SMALL UTILITIES)

O R D E R

On November 13, 1998, Airview Estates, Inc. (Airview) filed its application for Commission approval of proposed sewer rates. Commission Staff, having performed a limited financial review of Airview s operations, has prepared the attached Staff Report containing Staff's findings and recommendations regarding the 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 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 requests for 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 21st day of April, 1999.

By the Commission

ATTEST:

Executive Director

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the matter of:

THE APPLICATION OF AIRVIEW ESTATES,)
INC. FOR A RATE ADJUSTMENT PURSUANT) CASE NO. 98-595
TO THE ALTERNATIVE RATE FILING FOR)
SMALL UTILITIES)

STAFF REPORT

Prepared by: Karen S. Harrod, CPA
Public Utility Financial Analyst
Water and Sewer Revenue
Requirements Branch
Division of Financial Analysis

STAFF REPORT
ON
AIRVIEW ESTATES, INC.
CASE NO. 98-595

On November 13, 1998, Airview Estates, Inc. (Airview) filed its application seeking to increase its rates for sewer service. In order to evaluate the requested increase, Commission Staff (Staff) performed a limited financial review of Airview s test period operations, the year ending December 31, 1997.

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.

Karen Harrod of the Commission s Water and Sewer Revenue Requirements Branch began the limited review on January 14, 1999, and is responsible for the preparation of this Staff Report.

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

Attachment C compares Airview s and Staff s revenue requirement calculations. Airview determined its pro forma revenue requirement to be \$72,380, an increase over test year revenues of \$25,659, or 54.92 percent. Staff recommends a revenue requirement of \$57,367, which represents an increase of \$10,646 or 22.79 percent. The rate contained in Attachment D will achieve Staff s recommended level of revenue.

Staff anticipates that the recommended rate will generate sufficient revenues to allow the utility to meet all its cash operating expenses for the next three years. At the end of this three-year period, staff will perform a limited review of the utility's operations and notify the utility and Commission of any adjustments deemed necessary to ensure that the utility's rates remain adequate. As part of that review the utility may be required to file additional information.

The utility shall notify the Commission in writing if during this three-year period, and prior to the limited review, the revenues generated by the recommended rates become inadequate to meet its cash operating expenses.

Signature

Prepared by: Karen S. Harrod, CPA
Public Utility Financial Analyst
Water and Sewer Revenue
Requirements Branch
Division of Financial Analysis

ATTACHMENT A
STAFF REPORT CASE NO. 98-595
AIRVIEW ESTATES, INC. - REQUESTED OPERATIONS

	Test Year per Annual Report	Requested Adjustments	Requested Operations
Operating Revenues	40,757	5,964	46,721
Operating Expenses:			
Supervision	3,000		3,000
Labor & Exp.			
Collection System Expense	-		-
Pumping System Expense	-		-
Sludge Hauling	844		844
Utility Service - Water Cost	302		302
Other Labor, Materials, & Expenses	2,680		2,680
Fuel & Power Purchased	3,540		3,540
Chemicals	477		477
Routine Maintenance	6,000		6,000
Maintenance	14,715		14,715
Collection Expense	2,352	120	2,472
Office Expense	2,603		2,603
Outside Services	4,026		4,026
Insurance Expense	1,158		1,158
Transportation	148		148
Miscellaneous Expense	240		240
Depreciation Expense	1,113	1,305	2,418
Amortization Expense	602	17,123	17,725
Taxes Other than Income Taxes	1,108		1,108
Income Taxes	1,000	(768)	232
Interest	1,851	(1,851)	-
Penalties	2,088	(2,088)	-
Total Operating Expenses	<u>49,847</u>	<u>13,841</u>	<u>63,688</u>
Operating Income	<u>(9,090)</u>	<u>(7,877)</u>	<u>(16,967)</u>

ATTACHMENT B
STAFF REPORT CASE NO. 98-595
STAFF S RECOMMENDED OPERATIONS

	Test Year per Annual Report	Recommended Adjustments	Ref	Recommended Test Year
Operating Revenues	40,757	5,964	(a)	46,721
Operating Expenses:				
Supervision	3,000			3,000
Labor & Exp.				
Collection System Expense	-			-
Pumping System Expense	-			-
Sludge Hauling	844			844
Utility Service - Water Cost	302			302
Other Labor, Materials, & Expenses	2,680			2,680
Fuel & Power Purchased	3,540	321	(b)	3,861
Chemicals	477			477
Routine Maintenance	6,000			6,000
Maintenance	14,715			14,715
Collection Expense	2,352	120	(c)	2,472
Office Expense	2,603			2,603
Outside Services	4,026			4,026
Insurance Expense	1,158			1,158
Transportation Expense	148			148
Miscellaneous Expense	240	(240)	(d)	-
Depreciation Expense	1,113	1,305	(e)	2,418
Amortization Expense	602	5,665	(f)	6,267
Taxes Other than Income Taxes	1,108			1,108
Penalties	2,088	(2,088)	(g)	-
Total Operating Expenses	<u>46,996</u>	<u>5,083</u>		<u>52,079</u>
Operating Income	(6,239)	881		(5,358)
Interest Expense	<u>1,851</u>	<u>(1,851)</u>	(g)	<u>-</u>
NET INCOME	<u>(8,090)</u>	<u>2,732</u>		<u>(5,358)</u>

ATTACHMENT B
STAFF REPORT CASE NO. 98-595
STAFF S RECOMMENDED OPERATIONS

(a) Operating Revenues. Airview reported operating revenues of \$91,095 for the test year. Based on the current monthly rate of \$18.90 and the current number of customers of 206, Airview proposed to increase test year revenues to a normalized level of \$46,721. Staff agrees with this adjustment and has included the increase in the determination of Airview s revenue requirement.

(b) Fuel & Power Purchased. For the test year Airview reported \$3,540 in fuel and power purchased expense. Based on Staff s review the test year amount included only eleven months of electric invoices. Accordingly, Staff has made an adjustment to increase test year expense by \$321, to a level of \$3,861, to annualize the expense. The adjustment represents the average monthly expense incurred during the eleven-month period that was posted.

(c) Collection Expense. During the test year Airview incurred collection expense of \$2,352 for the billing and collection of sewer fees. Based on the cost of \$1.00 per month per customer and the current customer level of 206, Airview proposed to increase this expense to a level of \$2,472. Staff concurs with this increase of \$120 and has included it for ratemaking purposes.

(d) Miscellaneous Expense. Airview reported miscellaneous expense of \$240 for the test period. Based on staff s review this amount was paid to Chapel Hill United Church. Donations are not allowable expenses for ratemaking purposes. Therefore, staff has disallowed miscellaneous expense of \$240.

(e) Depreciation Expense. For the test year Airview reported depreciation expense of \$1,113. In its application an adjustment was proposed to increase this expense by \$1,305 based on the purchase and installation cost of \$6,525 for a new aerator,

ATTACHMENT B
STAFF REPORT CASE NO. 98-595
STAFF S RECOMMENDED OPERATIONS

depreciated over a period of 5 years. After consulting with Commission Engineering staff, it has been determined that the aerator is a necessary purchase and that five years is a reasonable depreciable life. As a result, the proposed adjustment has been included for ratemaking purposes.

(f) Amortization Expense. Airview reported amortization expense of \$602 in the test year for the amortization of rate case expenses incurred in Case No. 95-273.¹ Based on Airview's 1997 Annual Report, that expense was fully depreciated during 1997. Accordingly, test year amortization expense has been decreased by \$602.

In its application Airview proposed rate case expense amortization of \$725, based on office expenses of \$375 and accounting expenses of \$1,800, incurred for this proceeding. No invoices were provided to support the office expenses. As a result Staff recommends an increase in amortization expense of \$600 for the amortization of rate case related accounting expenses of \$1,800.

An additional adjustment proposed by Airview was the amortization of expenses to be incurred for the dredging, dewatering, and disposal of lagoon sludge. These procedures are needed to bring the sewage treatment plant into compliance with Commission regulations. In Case No. 98-129² the Commission ordered Airview to closely monitor the lagoon for overloading conditions and to dredge the lagoon before overloading occurs. The plant's most recent inspection by a Commission utility investigator took place on March 25 & 26, 1999. At that time it was noted that the

¹ In the Matter of the application of Airview Estates, Inc. for a rate adjustment pursuant to the alternative rate filing procedure for small utilities, November 20, 1995.

² In the Matter of an investigation of Airview Estates, Inc., December 21, 1998.

ATTACHMENT B
STAFF REPORT CASE NO. 98-595
STAFF S RECOMMENDED OPERATIONS

lagoon was already high in solids. According to the inspector, the lagoon should be dredged as soon as possible. Therefore, it is the opinion of Staff that Airview should take the appropriate measures to dredge the lagoon.

Bids were provided to support the estimated cost of \$85,000 for the dredging, dewatering, and removal of sludge and Airview proposed to amortize this expense over a period of five years. According to Mr. Larry Smither, whose consulting company provides management services for Airview, this is the first time an expense of this nature has been necessary since the plant was constructed in 1973. Ideally it will never recur, but in the event that it does, it is not likely to be necessary for another 15 - 20 years. After consulting with PSC engineering staff, it is recommended that the expenses to be incurred by Airview for dredging, dewatering, and disposal of lagoon sludge be amortized over a period of 15 years. This results in an increase to amortization expense of \$5,667.

Based on the aforementioned adjustments, Staff recommends a net increase to test year amortization expense of \$5,665 to a level of \$6,267.

(g) Penalties & Interest Expense. For the test year Airview reported penalties and interest expense of \$2,088 and \$1,851, respectively. An adjustment was proposed to eliminate these expenses for ratemaking purposes. Staff concurs with the proposed adjustments and has decreased both penalties and interest expense to a level of \$0.00.

ATTACHMENT C
 STAFF REPORT CASE NO. 98-595
 CALCULATION OF REQUESTED AND RECOMMENDED
 REVENUE REQUIREMENTS

	Requested by Airview	Recommended by Staff
Adjusted Operating Expenses	63,688	49,079
Operating Ratio		0.88
Required Operating Revenue before Income Taxes		55,772
Less: Adjusted Operating Expenses		49,079
Revenue Subject to Income Taxes		6,693
Gross-Up Factor		1.23839
Net Operating Income Inclusive of Provision for Income Taxes		8,288
Add: Adjusted Operating Expenses		49,079
Revenue Requirement	72,380	57,367
Less: Normalized Test-Year Revenue	46,721	46,721
Required Increase	25,659	10,646

ATTACHMENT D
STAFF REPORT CASE NO. 98-595
RECOMMENDED SEWER RATES

RECOMMENDED RATES

Single Family Residential

\$23.21 per Month