

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF FARMDALE DEVELOPMENT)
CORPORATION FOR AN ADJUSTMENT IN)
RATES PURSUANT TO THE ALTERNATIVE) CASE NO. 2007-00436
RATE FILING PROCEDURE FOR SMALL)
UTILITIES)

O R D E R

On October 3, 2007, Farmdale Development Corporation ("Farmdale") filed an application for Commission approval of its proposed sewer rates pursuant to the alternative rate filing procedure for small utilities. Commission Staff, having performed a limited financial review of Farmdale's operations, issued a Staff Report on February 11, 2008 containing its findings and recommendations regarding the proposed rates. Based upon the written comments received from the parties to this case, as well as the discussions from an informal conference held on March 27, 2008, Commission Staff has prepared an Amended Staff Report. All parties should review the report carefully and provide any written comments on Staff's findings and recommendations within 7 days from the date of this Order.

IT IS THEREFORE ORDERED that all parties shall have 7 days from the date of this Order to submit written comments regarding the attached Amended Staff Report.

Done at Frankfort, Kentucky, this 5th day of May, 2008.

By the Commission

ATTEST:


Executive Director

AMENDED STAFF REPORT
FARMDALE DEVELOPMENT CORPORATION
CASE NO. 2007-00436

On October 3, 2007, Farmdale Development Corporation ("Farmdale") filed its application seeking to increase its rates pursuant to 807 KAR 5:076. Farmdale's current rate is a flat monthly fee of \$28.00. Farmdale proposes to increase its current flat rate by 52.64 percent to \$42.75, which would produce increased revenues of \$42,653. In order to evaluate the requested increase, Commission Staff ("Staff") performed a limited review of Farmdale's test period operations for the year ending December 31, 2006. Based on its review, Staff issued a report on February 11, 2008 wherein a monthly rate of \$30.86 was recommended. Farmdale requested an informal conference to discuss the report.

A conference was held on March 27, 2008. Pursuant to discussions at the conference and information subsequent thereto, Staff is amending its original report and now recommends that the flat monthly rate be set at \$31.09 per customer. In addition, it should be noted, as requested by Intervenor Linda Ethington, that Farmdale's customers are also paying a surcharge of \$9.92 for five years from the date of its approval in Farmdale's previous rate case, which was decided on April 11, 2007.

Staff's adjustments to the pro forma operating statement as determined in Staff's original report are shown in Attachment A. Staff's revenue requirement and calculation of the recommended rate is shown in Attachment B.

Signatures

Prepared by: Jack Kaninberg
Financial Analyst, Water and Sewer
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Eddie Beavers

Prepared by: Eddie Beavers
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ATTACHMENT A
 AMENDED STAFF REPORT CASE NO. 2007-00436
 REVISED PRO FORMA OPERATIONS

| Farmdale Development Attachment A | Proforma from Staff Report of February 11, 2008 | Adjustments | Ref. | Staff Amended |
|--|--|-----------------------|-------------|----------------------|
| Flat-Rate Revenue | \$80,976 | | | \$80,976 |
| Owner/Manager fee | \$6,000 | | | \$6,000 |
| Sludge Hauling | \$2,600 | 0 | A | \$2,600 |
| Water Cost | \$1,622 | | | \$1,622 |
| Other-Labor, Matl, & Exp. | \$7,800 | | | \$7,800 |
| Fuel/Power for Pumping | \$15,303 | | | \$15,303 |
| Chemicals | \$2,402 | | | \$2,402 |
| Routine Mt. Fee | \$9,720 | | | \$9,720 |
| Mt.-Collection System | \$350 | | | \$350 |
| Mt. Of Trtmnt & Disp. | \$4,388 | \$598 | B | \$4,986 |
| Mt. of Other | \$1,008 | | | \$1,008 |
| Agency Collection Fee | \$8,097 | | | \$8,097 |
| Office Supplies/Other | \$278 | | | \$278 |
| Outside Serv. Employed | \$3,000 | | | \$3,000 |
| Insurance Expense | \$543 | | | \$543 |
| Reg. Commission Exp. | \$590 | | | \$590 |
| Miscellaneous Expense | \$26 | | | \$26 |
| Rents | \$600 | | | \$600 |
| <i>Total Sewer O&M</i> | <i>\$64,327</i> | <i>\$598</i> | | <i>\$64,925</i> |
| Depreciation Expense | \$3,433 | \$93 | C | \$3,526 |
| Amortization Expense | \$4,097 | (\$120) | D | \$3,977 |
| Taxes OT Income | \$1,142 | | | \$1,142 |
| Total Op. Expense | \$72,999 | \$571 | | \$73,570 |
| Income Taxes | \$175 | | | \$175 |
| Interest Expense | \$6,283 | | | \$6,283 |
| <i>Total Expense</i> | <i>\$79,457</i> | <i>\$571</i> | | <i>\$80,028</i> |
| <i>Net Income</i> | <i>\$1,519</i> | <i>(\$571)</i> | | <i>\$948</i> |

Explanatory Notes:

A. Sludge Hauling Expense – was originally adjusted by \$2,850 to reduce the 2006 sludge hauling expense of \$5,450 to the \$2,600 amount which was incurred in 2005 and allowed in Farmdale’s most recent rate case. The justification for this recommendation was that Farmdale’s sludge hauling expenses appear to have been abnormally high in 2006. This observation was based on a comparison of Farmdale’s reported expenses

both prior to and following the 2006 test period. Farmdale's historical sludge hauling costs have been as follows:

| Year | Sludge Hauling Expense |
|-------------|------------------------|
| 2002 | \$2,360 |
| 2003 | \$1,120 |
| 2004 | \$1,120 |
| 2005 | \$2,600 |
| 2006 | \$5,450 |

The Staff Report noted that subsequent to 2006, Farmdale paid sludge hauling expenses totaling \$1,975 through June 30, 2007. However, of that amount \$1,550 was actually incurred for service rendered in November and December 2006, leaving only \$425 in expense for sludge hauling done and paid for in the first six months of 2007. These factors suggested to Staff that the sludge hauling expense for 2006 was abnormally high.

In response to the Staff Report, Farmdale provided evidence that the sludge hauling expense for 2007 was \$4,250, which is lower than its 2006 expense but higher than the amount recommended by Staff based on its trend analysis. Farmdale also stated that at least two loads of sludge were removed and processed at no charge to Farmdale, although it did not estimate the cost of those loads.

The evidence recently provided by Farmdale suggests that the normal sludge hauling expense needed to properly maintain the plant may be greater than \$2,600, although the 2006 expense of \$5,450 is still higher than the amounts experienced both in prior years and in 2007. One alternative would be to allow Farmdale the 2007 amount of \$4,250. Another alternative would be to allow a three-year average of the total expense of \$12,300 for 2005 through 2007, which would result in a pro forma expense of \$4,100.

In fairness to all parties, Farmdale should provide additional evidence relative to its ongoing sludge hauling costs to give the Commission the information needed to render an informed decision. Specifically, Farmdale at the hearing in this matter should provide the 2008 bills for sludge hauling expense up to the date of the hearing.

B. Maintenance of Treatment and Disposal Expenses –The Staff Report recommended that a survey of sewer mains and manholes costing \$597.52 be removed from test period operations and recovered in Amortization Expense over a five-year period. In response, Farmdale has provided evidence that the survey is performed annually. Therefore, Staff recommends that this expense be fully included in operations and recovered annually.

C. Depreciation Expense – The Staff Report recommended depreciation expense of \$233.61 to allow a seven-year recovery for a motor installation costing \$1,635.29 which was removed from Maintenance of Treatment/Disposal Expense. Farmdale argued for

recovery of this expenditure over five years, a difference of \$93, because of the labor costs involved. Staff recommends accepting this adjustment.

D. Amortization Expense - was originally adjusted by \$119.51 to allow a five-year recovery for the survey of mains and manholes. Because Farmdale has argued that this is an annual expenditure, and Staff has accepted this argument, Amortization Expense should be reduced accordingly.

ATTACHMENT B
AMENDED STAFF REPORT CASE NO. 2007-00436
STAFF'S RECOMMENDED REVENUE REQUIREMENT AND RATE

Calculation of Revised Revenue Requirement using Operating Ratio Method:

| | |
|--------------------|---|
| \$ 73,570 | Revised Proforma Operating Expenses |
| <u>88%</u> | Operating Ratio |
| \$ 83,603 | Subtotal |
| \$ 6,283 | Plus Recommended Interest Expense |
| \$ 89,886 | Revenue Requirement |
| <u>(\$ 80,976)</u> | Less Normalized Revenues |
| \$ 8,910 | Recommended Revenue Increase (11% Increase) |

$\$89,886 / 12 = \$7,490.50$ divided by 241 customers = $\$31.0809$ per month bill

Recommended Monthly Rate (rounded up)

\$31.09