

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF RIVER ROAD DISPOSAL)
SYSTEM FOR AN ADJUSTMENT OF RATES) CASE NO. 2011-00458
PURSUANT TO THE ALTERNATIVE RATE)
FILING PROCEDURE FOR SMALL UTILITIES)

NOTICE OF FILLING OF COMMISSION STAFF REPORT

Notice is hereby given that, in accordance with the Commission's Order of December 22, 2011, the attached report containing the findings and recommendations of Commission Staff regarding the Applicant's proposed rate adjustment has been filed in the record of the above-styled proceeding.



Jeff Derouen
Executive Director
Public Service Commission
P.O. Box 615
Frankfort, KY 40602

DATED: FEB 01 2012

cc: Parties of Record

STAFF REPORT
ON
RIVER ROAD DISPOSAL SYSTEM
CASE NO. 2011-00458

On December 19, 2011, River Road Disposal System (“River Road”) filed an application with the Commission to adjust its current rate for sewer service.¹ Using its historical operations for the calendar year ending December 31, 2010 and adjusting for known and measureable changes, River Road proposes to increase its monthly rate for service from \$39.28 to \$57.38, an increase of approximately 46.1 percent. The proposed rates will produce additional annual revenues of \$2,172.

Daryl Parks and Sam Reid of the Commission’s Division of Financial Analysis performed a limited financial review of River Road’s test-year operations to determine whether test-period operating revenues and expenses are representative of normal operations and the proposed adjustments are reasonable. They did not pursue, nor have they addressed in this report, insignificant or immaterial discrepancies. Where they have not expressly addressed a test-period expense, they found insufficient evidence to contest the reasonableness of that expense.

This report summarizes Commission Staff’s review and recommendations. Mr. Reid reviewed River Road’s operating revenue calculations and its calculation of the proposed rate. Mr. Parks addresses all pro forma expense adjustments and the revenue requirement determination. River Road’s pro forma operating income

¹ River Road tendered its application for rate adjustment to the Commission on November 28, 2011. Due to certain deficiencies in the filing, the Commission did not accept the application. On December 19, 2011, River Road cured these deficiencies and the Commission accepted its application.

statement is set forth in Appendix A. In Appendix B, Commission Staff explains each of its proposed pro forma adjustments.

Commission Staff recommends that the operating ratio methodology be used to calculate River Road's revenue requirement.² This approach is used when no basis for a rate-of-return determination exists, the cost of the utility has fully or largely been funded through contributions, or the utility has little or no outstanding long-term debt. Commission Staff is of the opinion that an operating ratio of 88 percent will allow River Road sufficient revenues to cover its reasonable operating expenses and provide for reasonable equity growth. As shown in Table 1, applying an 88 percent operating ratio to requested pro forma operations produces a revenue requirement from rates of \$6,886.16, an increase of \$2,172.56, or 46.09 percent above the normalized revenue from rates of \$4,713.60.

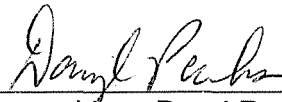
Table I: Revenue Requirement Determination	
Net Pro Forma Operating Expenses	\$ 6,059.82
Divided by: Operating Ratio	÷ 88%
Subtotal	\$ 6,886.16
Add: Interest Expense	+ 0
Total Revenue Requirement	\$ 6,886.16
Less: Other Income & Deductions	- 0
Revenue Requirement from Operations	\$ 6,886.16
Less: Other Operating Revenues	- 0
Revenue Requirement - Water Sales	\$ 6,886.16
Less: Pro Forma Revenue - Water Sales	- 4,713.60
Requested Increase	\$ 2,172.56
Percentage Increase	46.088%

² Operating Ratio is the ratio of expenses, including depreciation and taxes, to gross revenues. It is illustrated by the following equation:

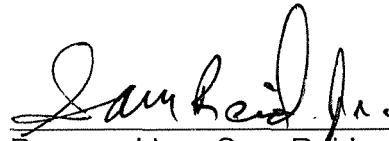
$$\text{Operating Ratio} = \frac{\text{Operating Expenses} + \text{Depreciation} + \text{Taxes}}{\text{Gross Revenues}}$$

Commission Staff's recommended revenue requirement will allow River Road to cover its pro forma operating expenses and provide for future equity growth. Based upon the number of customers that River Road presently serves, the proposed monthly rate of \$57.38 will produce annual revenues of approximately \$6,886. Therefore, Staff recommends that the Commission accept that rate.

Signatures



Prepared by: Daryl Parks
Financial Analyst, Water and Sewer
Revenue Requirements Branch
Division of Financial Analysis



Prepared by: Sam Reid
Rate Analyst, Communications, Water
and Sewer Rate Design Branch
Division of Financial Analysis

APPENDIX A
STAFF REPORT, CASE NO. 2011-00458
PRO FORMA OPERATIONS

	2010 <u>Annual Report</u>	Proposed <u>Adjustment</u>	Adj. <u>Ref.</u>	Pro Forma <u>Operations</u>
Operating Revenues:				
Revenue	\$ 4,713.60	\$ 0		\$ 4,713.60
Operating Expenses:				
Operation & Maintenance:				
Pumping System	\$ 290.00	\$ 0		\$ 290.00
Water Cost	184.17	(13.77)	A	170.40
Water Testing	460.16	13.92	B	474.08
Purchased Power	711.25	0		711.25
Chemicals	193.35	0		193.35
Maintenance Fee	2,462.47	237.53	C	2,700.00
Pumping System	508.80	(508.80)	D	0
Offices Supplies and				
Expenses	139.27	0		139.27
Regulatory Commission				
Expense	200.00	0		200.00
Miscellaneous Expenses	300.00	0		300.00
Total Operation &				
Maintenance	\$ 5,449.47	\$ (271.12)		\$ 5,178.35
Depreciation	300.00	50.81	E	350.81
Amortization	0	440.00	F	440.00
Taxes Other Than Income:				
Payroll Taxes	0	0		0
PSC Assessment	90.66	0		90.66
Utility Operating Expenses	\$ 5,840.13	\$ 219.69		\$ 6,059.82
Net Utility Operating Income	\$ (1,126.53)	\$ (219.69)		\$ (1,346.22)
Other Income & Deductions:				
Interest Income	0	0		0
Interest Expense	0	0		0
Net Income Available for Debt				
Service	<u>\$ (1,126.53)</u>	<u>\$ (219.69)</u>		<u>\$ (1,346.22)</u>

APPENDIX B
STAFF REPORT, CASE NO. 2011-00458
EXPLANATION OF PROPOSED ADJUSTMENTS

A. Water Cost: In an average month, River Road's water usage falls within the usage amount allowed for the minimum bill assessed by Paintsville Utilities. This usage equates to a monthly bill of \$14.20, or a yearly cost of \$170.40, which is \$13.77 less than the cost incurred in the test year. River Road's water cost expense should be reduced by \$13.77.

B. Water Testing: Currently, River Road pays McCoy & McCoy \$118.52 every 3 months for water testing. This quarterly expense yields a normalized annual expense of \$474.08. This amount is an increase of \$13.92 over the test year expense. Water testing expense should be increased by \$13.92.

C. Maintenance Fee: The certified operator who River Road currently employs increased his monthly fee to \$225. This action results in a normalized yearly expense of \$2,700, an increase of \$237.53 over the test year expense. Therefore, River Road's maintenance fee expenses should be increased by \$237.53.

D. Pumping System: During the test year, River Road installed new grates. It expensed this cost instead of capitalizing it. This cost should be depreciated and removed from the pumping system account.

E. Depreciation: The cost of installing new grates was originally expensed in the pumping system account. River Road proposes to remove the cost from that account and to depreciate the \$508.08 expense over 10 years, or \$50.81 per year. Commission Staff concurs with the proposed action and recommends that depreciation expense be increased by \$50.81.

F. Amortization: River Road incurred a cost of \$2,200 to renew its Kentucky Pollutant Discharge Elimination System permit during the test year. This permit is effective for a period of five years. River Road proposes to amortize the cost of this permit over the life of the permit. The yearly-amortized expense would be \$440. Amortization expense should be increased by \$440.

Marsha Cantrell
River Road Disposal Systems
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