

COMMONWEALTH OF KENTUCKY
BEFORE THE UTILITY REGULATORY COMMISSION

* * * * *

In the Matter of:

NOTICE OF ADJUSTMENT OF RATES)
OF GLENGARRY UTILITIES, INC.)
d/b/a ZELMA FIELDS SEWAGE) CASE NO. 7593
TREATMENT PLANT TO BECOME)
EFFECTIVE ON OCTOBER 20, 1979)

O R D E R

Preface

On September 28, 1979, Glengarry Utilities, Inc., d/b/a Zelma Fields Sewage Treatment Plant, hereinafter referred to as the "Utility", filed with this Commission a duly verified application seeking an adjustment of its sewage rate, proposing an effective date of October 20, 1979.

The case was set for hearing at the Commission's Offices in Frankfort, Kentucky on December 13, 1979. Subsequent hearings were held on January 22, 1980, February 5, 1980 and February 26, 1980. All parties of interest were notified with the Consumer Protection Division of the Attorney General's Office and Zelma Fields Subdivision residents, by counsel, permitted to intervene in the matter. At the hearings, certain requests for additional information were made by the Commission Staff.

Pursuant to the conclusion that all requested information and other pertinent matters have been filed, the entire matter is now considered to be fully submitted for a final determination by this Commission.

Test Period

The Utility has selected the twelve month period ending June 30, 1979, as the "Test-Year" and has submitted tabulations of its revenues and expenses for this period including its proforma adjustments thereto for the Commission's consideration in the deter-

mination of rate adjustments. Said tabulations along with those found reasonable by this Commission are included in Appendix "C" of this Order.

Rate Determination

While the Commission has traditionally considered the original cost of utility plant, the net investment, the capital structure, and the cost of reproduction as a going concern in the determination of fair, just, and reasonable rates its experience in the establishment or adjustment of rates for sewage utilities has indicated that these valuation methods are not always appropriate. Sewage utilities are unique to the extent that the cost of facilities has usually been included in the cost of the individual lot. The owner and/or operator of the utility is, in many instances, the developer of the real estate and title may have changed hands prior to the effective date of Commission jurisdiction (January 1, 1975). Further, the Commission has found that the books, records and accounts of these utilities are, for the most part, incomplete, so as to make impossible the fixing of rates on the above methods of valuation. The Commission is, therefore, of the opinion that the "Operating Ratio Method"⁽¹⁾ should be utilized in rate-making determinations for sewage utilities although it is recognized that there may be instances where the method would not be valid.

Findings In This Matter

The Commission, after consideration of all the evidence of record and being advised, is of the opinion and finds:

1. That, in this instance, the determination of rates and revenue requirements should be based on the operating ratio method.
2. That the rate prescribed and set forth in Appendix "A", attached hereto and made a part hereof, is the fair, just, and reasonable rate to be charged for sewage services rendered by the Utility, in the Zelma Fields Subdivision of Jefferson County, Kentucky.

(1) Operating ratio is defined as the ratio of expenses, including depreciation and taxes to gross revenues.

$$\text{Operating Ratio} = \frac{\text{Operating Expenses} + \text{depreciation} + \text{taxes}}{\text{Gross Revenues}}$$

3. That an operating ratio of 0.88 results from the projected operations as adjusted and provides a reasonable return margin⁽²⁾ in this instance. Further, that interest expenses associated with long and short term debt should not be included in computing the operating ratio.

4. That the rate proposed by the Utility is unfair, unjust, and unreasonable in that it would produce revenues in excess of those found reasonable herein and should be denied.

5. That the Utility has filed with this Commission a valid third-party beneficiary agreement.

6. That while traditionally depreciation on contributed property for rate-making purposes has been allowed, it has not been a matter of great significance in past years. The value of contributed property in currently operating water and sewage utilities, however, is frequently more than the value of investor financed property. Further, it is common practice for a builder or developer to construct water and sewage facilities that add to the value and salability of his subdivision lots and to expense this investment cost in the sale price of these lots or, as an alternative, to donate these facilities to a utility company.

It is also recognized that many residential and commercial developments in metropolitan areas are served by privately-owned sewage systems. Further, that federal guidelines will require the incorporation of these sewage systems into a regional comprehensive sewer district at such time as connecting trunk lines are made available. Further, that to permit the accumulation of a depreciation reserve on contributed property that is to be abandoned would not, in our opinion, be in the public interest.

The Commission is, therefore, of the opinion and finds that depreciation on contributed property for water and sewage utilities is not justified and should not be included in rate-making determinations for these utilities. In support of this position and by way of substantiation, we make reference to the cases and decisions listed in Appendix "B", attached hereto and made a part hereof.

(2) Return margin is the amount remaining for the payment of a return on the investment of the security holders.

7. That the Commission, after consideration of the tabulation of test-year and projected revenues and expenses submitted by the Utility, concludes that these revenues, expenses and adjustments can be summarized as shown in Appendix "C", attached hereto and made a part hereof. On the basis of the said Appendix "C" tabulation, the Commission further concludes that annual revenues in the amount of \$39,750 are necessary and will permit the Utility to meet its reasonable expenses for providing sewage collection and disposal service to 250 customers.

Orders In This Matter

The Commission, on the basis of the matters hereinbefore set forth and the evidentiary record in this case:

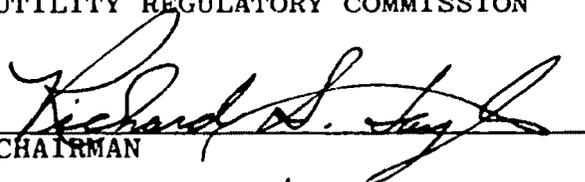
HEREBY ORDERS that the rate prescribed and set forth in Appendix "A", attached hereto and made a part hereof be and they are hereby fixed as the fair, just, and reasonable rate of the Utility for providing sewage disposal services to customers located in the Zelma Fields Subdivision, Jefferson County, Kentucky, to become effective for services rendered on and after the date of this Order.

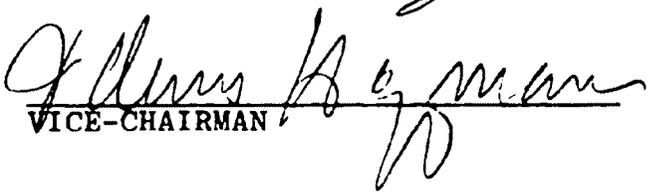
IT IS FURTHER ORDERED that the rate sought by the Applicant be and the same are hereby denied.

IT IS FURTHER ORDERED that the Utility file with this Commission, within thirty (30) days from the date of this Order, its tariff sheets setting forth the rate approved herein. Further that a copy of the Utility's Rules and Regulations for providing service to its customers shall be filed with said tariff sheets.

Done at Frankfort, Kentucky, this 24th day of March, 1980.

UTILITY REGULATORY COMMISSION


CHAIRMAN


VICE-CHAIRMAN


COMMISSIONER

ATTEST:

SECRETARY

APPENDIX "A"

APPENDIX TO AN ORDER OF THE UTILITY REGULATORY
COMMISSION IN CASE NO. 7593 DATED MARCH 24, 1980

The following rates are prescribed for sewage disposal services rendered to all residential customers served by the Zelma Fields Sewage Treatment Plant, in Zelma Fields Subdivision, in Jefferson County, Kentucky:

<u>Type of Service Provided</u>	<u>Monthly Rate</u>
Single-Family Residential	\$13.25 Per Residence

APPENDIX "B"

APPENDIX TO AN ORDER OF THE UTILITY REGULATORY
COMMISSION IN CASE NO. 7593 DATED MARCH 24, 1980

A listing of cases and decisions that substantiate finding
number 6.

- (1) 28 U.S.C. s 362(c) (1976).

Dealing with the Basis to Corporations in Reorgani-
zation. It states in part that property contributed
by nonstockholders to a corporation has a zero basis.

- (2) Easter v. C.I.R., 338 F.2d 968 (4th Cir. 1964).

Taxpayers are not allowed to recoup, by means of de-
preciation deductions, an investment in depreciable
assets made by a stranger.

- (3) Martigney Creek Sewer Co., (Mo. Pub. Serv. Comm.,
Case No. 17,117) (November 26, 1971).

For rate making purposes a sewer company should not
be allowed to treat depreciation on contributed plant
as an operating expense.

- (4) Re Incline Village General Improv. Dist., I & S 558,
I & S 559, (Nev. Pub. Serv. Comm., May 14, 1970).

Where a general improvement district sought to in-
crease water rates, the Commission could not consider
depreciation expense on the district's plant because
all of the plant had been contributed by members of
the district.

- (5) Princess Anne Utilities Corp. v. Virginia ex. rel.
State Corp. Commission, 179 SE 2d 714, (Va. 1971).

A depreciation allowance on contributions in aid of
construction was not allowed to a sewer company
operating in a state following the "original cost"
rule in determining rate base because the company
made no investment in the property, and had nothing
to recover by depreciating the donated property.

APPENDIX "C"

APPENDIX TO AN ORDER OF THE UTILITY REGULATORY
COMMISSION IN CASE NO. 7593 DATED MARCH 24, 1980

In accordance with Finding No. 7, the following tabulation is the Commission summary of the "Test-Year" and projected annual revenues and expenses for the Utility's 100,000 GPD sewage collection and treatment system for providing service to test-year and proforma customers.

	Test Year ⁽¹⁾ Ending 6/30/79	Proforma ⁽¹⁾ Requested	Proforma Found Reasonable
(No. of Customers)	(250)	(250)	(250)
<u>Revenues:</u>	\$ 15,102	\$ 44,100	\$ 39,750
<u>Expenses:</u>			
1. Administrative & General			
a) Tax and License	\$ 288	\$ 288	\$ 288
b) Printing	128	128	128
c) Bookkeeping	1,200	1,200	1,200
d) Director's Fees	1,800	1,800	1,200 ⁽²⁾
e) Rent	600	600	600
2. Billing & Collecting			
a) Collection Charges	725	1,125	1,125
b) Bad Debts	20	45	20 ⁽³⁾
3. Operation & Maintenance			
a) Plant Supplies	517	569	517 ⁽³⁾
b) Repairs	8,233	9,056	8,233 ⁽³⁾
c) Utilities - Electric	5,192	5,712	5,192 ⁽³⁾
d) Utilities - Water	938	938	938
e) Sludge Hauling	2,380	3,255	2,618 ⁽⁴⁾
f) Service Contract	4,780	5,460	5,460
g) Health Dept. Fees	700	700	700
h) Water Analysis	-0-	160	160
4. Professional Services			
a) Legal			
1. Recurring	-0-	150	-0- ⁽³⁾
2. Rate Case	-0-	500	500 ⁽⁵⁾
b) Engineering			
1. Recurring	-0-	150	-0- ⁽³⁾
2. Rate Case # 6893	133	-0-	-0-
3. Rate Case # 7593	-0-	444	444 ⁽⁵⁾
c) Accounting			
1. Recurring	315	350	315 ⁽³⁾
2. Rate Case	-0-	250	250 ⁽⁵⁾
5. Depreciation	764	895	764 ⁽⁶⁾
6. Insurance	289	289	289
7. Financing			
a) Finance Charges	1,515	-0-	-0-
b) Interest Expense (Short Term)	-0-	2,216	2,216
c) Interest Expense (Long Term)	1,309	1,100	1,100
8. State & Federal Tax	-0-	1,405	1,116 ⁽⁷⁾
Total Expenses	\$ 31,826	\$ 38,785	\$ 35,373
Net Income (Loss)	(\$ 16,724)	\$ 5,315	\$ 4,377

FOOTNOTES TO APPENDIX "C"

CASE NO. 7593

1. Test Year and Proforma Requested Income and Expenses were taken from the Applicant's Comparative Income Statement for the twelve (12) month period ending June 30, 1979.
2. The Applicant's request for \$1,800 for Director's Fees has been reduced to \$1,200 based on previous allowances for comparable utilities operating in Jefferson County.
3. The Proforma Requested Expenses were reduced to the test-year amounts as the record in this matter failed to justify the requested increases.
4. The proforma allowance of \$2,618 for sludge hauling is based on 28 loads in the test year x \$85/present charge per load + a \$6.50 increase dumping charge + a \$2 fuel increase.
5. Rate Case Expenses were amortized over a three (3) year period.
6. The Applicant's request for \$895 for depreciation was reduced to the test-year expense of \$764 based on Mr. Kottke's testimony. (Transcript of Evidence--February 5, 1980, P. 36)
7. State and Federal Tax Liability has been computed on the basis of the revenues made possible from the rates approved herein.