

COMMONWEALTH OF KENTUCKY
BEFORE THE ENERGY REGULATORY COMMISSION

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In the Matter of:

NOTICE TO ADJUST RATES BY)
DAVIS BRANCH GAS COMPANY) CASE NO. 7870
JOHNSON COUNTY, KENTUCKY)

O R D E R

On May 29, 1980, Davis Branch Gas Company (Applicant) filed a Notice with the Commission requesting an increase in rates to be effective on and after July 1, 1980. To determine the reasonableness of the proposed rates the Commission in an Order dated June 13, 1980, suspended the requested rates for a period of five (5) months on and after the effective date and scheduled a public hearing for July 14, 1980. Notice of such hearing was made by the Applicant in manners prescribed by Kentucky Revised Statutes and the Commission's rules.

The hearing was held as scheduled with the Attorney General's Division of Consumer Intervention, the only party intervening in the matter. At the conclusion of the hearing, following responses for additional information and interrogatories served on Dr. Paul B. Hall, the matter was submitted to the Commission for final determination.

Commentary

Davis Branch Gas Company is a gas distribution utility serving approximately fifty customers in Johnson County, Kentucky. Davis Branch purchases its gas from three sources, the City of Paintsville, K. White Trustee and wells owned by the stockholders of the Davis Branch Gas Company.

The issue of management's authority to propose and implement new rates without stockholder's approval has been raised in this proceeding, as the appointment of the new manager in 1977 was informal and didn't provide specific agreement as to the extent of authority. However, this issue has been resolved as the Commission has received proof from two of the owners representing a majority, that they do sanction an increase in rates.

Test Period

For purposes of testing the reasonableness of the proposed rates and charges the Commission has adopted the twelve (12) months ending February 29, 1980, as the test period in this matter. Adjustments, where proper and reasonable, have been included to more clearly reflect current operating conditions.

Valuation Methods

The Company's records are inadequate and sufficient detail, is not available to determine the net investment or capitalization of the Company. As the records are incomplete, it is impossible for the Commission to make rate determinations on the traditional methods and therefore, the Operating Ratio Method will be used herein.

Revenues & Expenses

Applicant proposed several adjustments to its Operating Statement to more clearly reflect current operating conditions. The Commission finds these adjustments proper and has accepted them for ratemaking purposes with the following exceptions:

(1) Applicant proposed to adjust legal expenses by \$500⁽¹⁾ to reflect the amortization of anticipated legal fees connected with a tentative proposal to transfer ownership of the system to the present manager. Although the record indicates that this transfer is authorized by one owner, Paul B. Hall, M.D., the Commission has received nothing from the other owners of the system nor formal application from the potential purchaser regarding this subject. Therefore, the application for formal ownership change is not firm and the Commission does not find that these charges should be borne by the ratepayers at this time.

(2) The Company proposed to include depreciation expense on the estimated restoration costs of the system. It is the Commission's opinion that the expense is improper, as neither financing or certification of construction has been finalized or approved and the adjustment is, therefore, not known or measurable.

(1) Applicant's Exhibit 1, page 1 of 3.

The Commission is, however, cognizant of the fact that the Applicant has not included any depreciation for the test period, as adequate plant records do not exist. Therefore, the Commission has made an adjustment to Applicant's operating statement to allow for annual depreciation expense attributable to plant additions, since 1977. Total additions during this period were \$4,150⁽¹⁾, which depreciated over a thirty (30) year useful life would result in annual depreciation expense of \$138.

(3) The Commission heard testimony during the hearing that Applicant has been providing free gas service to certain of its customers. It is the Commission's opinion that it is entirely unfair and unjust for the remainder of the ratepayers to subsidize this free service. As the record is unclear as to the actual value of this service, the Commission has based the cost of purchased gas on test year sales volumes, thereby eliminating all gas losses associated with this subsidy from the Applicant's cost of service. Therefore, the Commission has reduced Applicant's adjustment to purchased gas by \$467.⁽²⁾

(4) Applicant proposed to increase its expenses for administrative and general salaries by \$2,400⁽³⁾ on an annual basis. This adjustment represents an increase of approximately 100% above test period salaries and is in the Commission's opinion excessive and unreasonable and is therefore denied.

As stated before in this Order, Applicant serves only 50 customers in a small operating area. As such the Commission finds that the level of salaries expensed during the test period provides adequate compensation to the employees involved and more accurately matches the value of these services to the customers of the utility.

Moreover, the Commission has made one additional adjustment to delete \$200⁽⁴⁾ for meters that were improperly expensed and should have been capitalized. The depreciation on these meters is included in operations as described above.

(1) Company response to Information Requested, Filed July 28, 1980.

(2) $11,693 \text{ MCF} - 11,109 \text{ MCF} = 584 \text{ MCF} \times \$0.80/\text{MCF} = \$467.$

(3) Applicant's Exhibit 1, page 1 of 3.

(4) IBID.

Therefore, test year operations have been adjusted to produce the following results:

	<u>Actual</u> ⁽⁵⁾	<u>Adjustments</u>	<u>Adjusted</u>
Operating Revenue	\$5,555	\$ -0-	\$ 5,555
Operating Expenses	8,539	7,266	15,805
Operating (Loss)	(\$2,984)	(\$ 7,266)	(\$10,250)
Interest Expense	-0-	174	174
Net Income	<u>(\$2,984)</u>	<u>(\$ 7,440)</u>	<u>(\$10,424)</u>

Return

The Commission is of the opinion that the adjusted operating deficit is clearly unjust and unreasonable.

The Commission is of the opinion that a fair, just and reasonable operating ratio is 88% which will allow Davis Branch Gas Company to pay its operating expenses, service its debt and provide a reasonable surplus. Therefore, the Commission finds that the additional revenue required is \$13,223, and is the amount granted herein.

Summary

The Commission, after reviewing all the evidence of record and being advised is of the opinion and FINDS:

(1) That the schedule of rates and charges set out in Appendix "A" are the fair, just and reasonable rates to charge for gas service rendered by Davis Branch Gas Company in that based on test year conditions they will produce revenues of \$22,147.

(2) That the operating ratio of 88% is fair, just and reasonable in that it should permit Davis Branch Gas Company to pay its operating expenses, service its debt and provide a reasonable surplus.

(3) That the rates proposed by Davis Branch and set out in the Notice should be denied in that they will produce annual revenues in excess of those found reasonable herein.

(4) That Applicant should immediately establish and maintain adequate plant and other balance sheet records and accounts in accordance with the Uniform System of Accounts for Class C and D gas companies.

(5) Applicant's Exhibit 1, page 1 of 3.

(5) That the Commission disapproves the Company's practice of granting certain customers free or reduced cost gas service, and that this practice is contrary to state law.

(6) That Applicant should cease granting no cost or reduced rate gas service in accordance with the provisions outlined in KRS 278.170.

IT IS THEREFORE ORDERED:

(1) That the schedule of rates and charges set forth in Appendix "A" are fair, just and reasonable for gas service rendered by Davis Branch Gas Company on and after the date of this Order.

(2) That the rates proposed by Davis Branch Gas Company and set out in the Application insofar as they differ from those in Appendix "A" be and are hereby denied.

(3) That Davis Branch Gas Company file with this Commission within thirty (30) days from the date of this Order its revised tariff sheets setting out the rates approved herein.

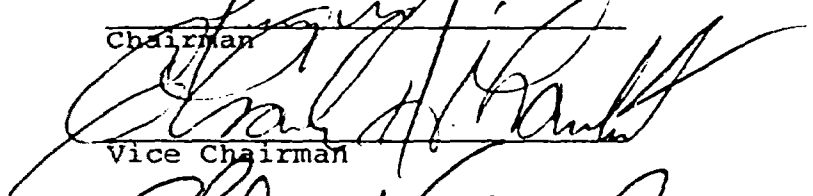
(4) That Applicant shall establish and maintain adequate plant and other balance sheet records and accounts in accordance with the Uniform System of Accounts for Class C and D gas companies.

(5) That Applicant shall cease granting no cost or reduced rate service in accordance with the provisions outlined in KRS 278.170.

Done at Frankfort, Kentucky, this 20th day of October, 1980.

ENERGY REGULATORY COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Secretary

APPENDIX "A"

APPENDIX TO AN ORDER OF THE ENERGY REGULATORY
COMMISSION IN CASE NO. 7870 DATED October 20, 1980

The following rates and charges are prescribed for the customers in the area served by Davis Branch Gas Company. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under the authority of the Commission prior to the date of this Order.

Gas Service

Rate:

0 to 1 mcf	\$3.00 per mcf
Over 1 mcf	\$1.62 per mcf

Minimum Bill:

First mcf	\$3.00
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