COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

ADJUSTMENT OF RATES OF HENDERSON-UNION RURAL ELECTRIC COOPERATIVE CORPORATION TO PROVIDE ADEQUATE REVENUES FOR ITS OPERATIONS AND CHANGE IN ENERGY REQUIREMENT FOR TWO CATEGORIES OF SERVICES AND IN MANNER OF BILLING	)	CASE NO. 8184

O R D E R

On March 31, 1981, Henderson-Union Rural Electric Cooperative Corporation ("Applicant") filed its notice of a general adjustment of rates and its proposal to change the energy requirement for two categories of service and the manner of billing for security lamps and street lights, to become effective as of 12:01 a.m. Central Standard Time, on May 1, 1981. The proposed rates would produce additional revenue of approximately $629,860 annually, an increase of 3.7% based on a normalized revenue derived from sales to rural system consumers. Applicant stated that the proposed adjustment of rates was necessary to generate sufficient income to carry on its operation and furnish adequate, safe, and reliable electric service to its member consumers; to meet the increasing expenses of operation; to have adequate reserves and an acceptable return on its investment and capital structure; and to have sufficient earning ratios to meet the requirements of its lenders and the mortgages securing its long-term debt.

The Commission issued an Order on April 1, 1981, which suspended the proposed rate increase for a period of five months, or until October 1, 1981. On May 14, 1981, the Commission issued an additional Order which scheduled a hearing for July 30, 1981, and directed Applicant to provide statutory notice to its consumers of the proposed rate increase and the scheduled hearing.

On April 7, 1981, the Division of Consumer Protection in the Office of the Attorney General filed a motion to intervene in this proceeding, which was sustained. This was the only party of interest formally intervening herein.

The hearing was conducted as scheduled at the Commission's offices in Frankfort, Kentucky, with all parties of record in attendance.

COMMENTARY

Henderson-Union Rural Electric Cooperative Corporation is a consumer-owned electric distribution cooperative serving approximately 14,220 consumers in the western Kentucky counties of Caldwell, Crittenden, Henderson, Hopkins, Lyon, Union, and Webster. Applicant receives all of its power requirements from Big Rivers Electric Corporation.

TEST YEAR

Applicant proposed, and the Commission has accepted, the 12-month period ending December 31, 1980, as the test period for determining the reasonableness of the proposed rates. In utilizing the historic test period, the Commission has given full consideration to known and measurable adjustments, where found reasonable.

VALUATION

Net Investment

The Commission finds from the evidence of record that Applicant's net investment rate base at December 31, 1980, is as follows:

Utility Plant in Service	$ 20,672,043
Construction Work in Progress	$ 864,979
Total Utility Plant	$ 21,537,022
Add:	
Materials and Supplies	$ 1,039,572
Prepayments	$ 42,594
Working Capital	$ 301,337
Sub-Total	$ 1,383,503
Deduct:	
Depreciation Reserve	$ 4,786,665
Customer Advances for Construction	$ 80,015
Sub-Total	$ 4,866,680
Net Investment	$ 18,053,845

In calculating the net investment rate base, the Commission has adjusted Materials and Supplies, as well as Prepayments, to utilize the 13-month average. The Commission has also adjusted the provision for working capital to include one-eighth of out-of-pocket operation and maintenance expenses, exclusive of any portion of the purchased power costs. The Commission finds, as

Applicant contended, that the time between payment of Applicant's power bill and receipt of revenues from its rural customers is a factor in the determination of the need for working capital. However, this evidence is not totally conclusive and other factors must be considered. Therefore, in the absence of any persuasive evidence to the contrary, the Commission is of the opinion that a departure from past policy is unwarranted and will allow only the one-eighth of out-of-pocket operation and m. intenance expenses, exclusive of purchased power. In addition, the Commission has adjusted the Depreciation Reserve to reflect the pro forma adjustment to depreciation expense found reasonable herein. Also, Applicant's rate base has been adjusted to reflect the exclusion of Customer Advances for Construction. The Commission is of the opinion that these advances are the equivalent of contributions of capital and, as such, should be excluded from the rate base.

Capital Structure

The Commission finds from the evidence of record that Applicant's capital structure for rate-making purposes is as follows:

Equity	$ 3,075,255
Long Term Debt	$ 17,114,184
Total Capitalization	$ 20,189,439

In conformity with past policy, the Commission has adjusted Applicant's proposed capital structure to exclude the increase in equity projected as a result of the request for increased rates.

The Commission has given due consideration to these and other elements of value in determining the reasonableness of the rate increase requested herein.

REVENUES AND EXPENSES

Applicant proposed several adjustments to revenues and expenses as reflected on Applicant's statement of operations shown on page 4 of the retail rate study attached to the application. The Commission finds that the adjustments proposed by Applicant are generally acceptable for rate-making purposes with the following modifications:

1. Applicant proposed an adjustment of $59,013 to depreciation expense. In determining the adjusted depreciation expense, Applicant utilized the value of plant in service at the end of the test year plus construction work in progress. The Commission has reduced the proposed adjustment by $26,814 to exclude depreciation on construction work in progress. In the absence of a corresponding adjustment to revenue to reflect the additional plant, the Commission finds that an adjustment to expense is improper and unacceptable.

2. Applicant proposed an adjustment of $20,007 to eliminate, for rate-making purposes, other capital credits. Applicant argued that these credits are of no economic value in that there is no reason to expect any future cash payments for them. The record indicates that the majority of these credits were assigned by the National Rural Utilities Cooperative Finance Corporation ("CFC").

The Commission does not find sufficient evidence in the record to support Applicant's contention that the capital credits assigned by associated organizations are not of economic value to the utility. Furthermore, the Commission is aware of the fact that CFC is presently retiring these credits on a 7-year cycle, which would provide an actual cash benefit to Applicant. Therefore, the Commission has adhered to its established policy and restored other capital credits of $20,007 as an item of income for rate-making purposes.

3. The Commission has eliminated Applicant's other income deductions of $4,160, for rate-making purposes, to exclude the cost of charitable contributions and donations incurred during the test year. The Commission is of the opinion and finds that these expenditures produce little or no benefit to Applicant's ratepayers and, therefore, should not be included for rate-making purposes.

The effect on net income of the revised pro forma adjustments is as follows:

	Actual Test Period	Pro Forma Adjustments	Adjusted Test Period
Operating Revenues	$73,378,556	$16,453,760	$89,832,316
Operating Expenses	72,515,148	16,501,002	89,016,150
Operating Income	$ 863,408	$ (47,242)	$ 816,166
Interest-Long Term Debt	637,343	210,751	848,094
Other Income and (Deductions)-Net	2,103,175	(2,011,176)	91,999
Net Income	$ 2,329,240	$(2,269,169)	$ 60,071

RATE OF RETURN

The actual rate of return for the test year on Applicant's net investment, established herein, was 4.78%. After taking into consideration the pro forma adjustments, Applicant would realize a 4.52% rate of return. The Commission is of the opinion and finds that the revised rate of return is inadequate and would impair Applicant's financial integrity. In order to remain on a sound financial basis, Applicant should be allowed to increase its annual revenue by approximately $629,860 which would result in a rate of return of 8.01% and a Times Interest Earned Ratio, excluding G & T capital credits, of 1.81.. This additional revenue will provide net income of approximately $689,931 which should be sufficient to meet the requirements in Applicant's mortgages, securing its long-term debt.

RATE DESIGN AND CLASSIFICATION

Applicant proposed increasing revenue from all non-contract rate classes by 3.7% which is the overall amount of increase in revenue derived from these customers. The Commission is of the opinion and finds Applicant's distribution of revenue among the various rate classes to be fair and equitable. However, the Commission has changed the allocation of revenue within the individual rate classes in two categories, residential and small commercial. Applicant proposed increasing its customer charges by approximately 11.0%, compared to the overall increase of 3.7%. The Commission finds that the evidence of record does not adequately support Applicant's proposed allocation of residential and small commercial revenues. Therefore, the Commission has adjusted the rates for residential and small commercial service whereby the increase in revenues will be more evenly distributed among all consumers.

Applicant proposed changes in its energy requirement in two categories of service and in the manner of billing for security lamps and street lights. The Commission is of the opinion and finds these changes to be proper and appropriate; therefore, they are reflected in Appendix A along with the other changes described herein.

The Applicant also proposed an increase of 0.02 mills per KWH to the Anaconda Aluminum Company ("Anaconda") energy charge. At the hearing the Applicant submitted a letter it had received from Anaconda objecting to this proposed increase. However, Anaconda did not formally intervene in the proceeding or provide information to support its allegations. Therefore, the Commission has accepted the Applicant's proposed changes to Anaconda's energy charge.

SUMMARY

The Commission, after consideration of the evidence of record and being fully advised, is of the opinion and finds that the rates and charges set out in Appendix A, attached hereto and made a part hereof, will produce gross annual revenue from sales in the amount of $90,289,868 and are the fair, just and reasonable rates for Applicant. The revenue from sales when added to other operating revenue will provide gross annual operating revenue of $90,462,176.

The Commission further finds that the rates and charges proposed by Applicant for residential and small commercial customers are unfair, unjust and unreasonable in that they place an unfair portion of the revenue increase on the low usage consumer.

IT IS THEREFORE ORDERED that the rates and charges set out in Appendix A, attached hereto and made a part hereof, are approved for service rendered on and after the date of this Order.

IT IS FURTHER ORDERED that the rates and charges proposed by Henderson-Union Rural Electric Cooperative Corporation for residential and small commercial customers are inadequately supported by the evidence of record and are hereby denied.

IT IS FURTHER ORDERED that Henderson-Union Rural Electric Cooperative Corporation shall file within 30 days from the date of this Order its revised tariff sheets setting out the rates approved herein.

Done at Frankfort, Kentucky, this 11th day of September, 1981.

PUBLIC SERVICE COMMISSION

Marlin M. Volz
Chairman

Katherine Randall
Vice Chairman

Leme Carregan
Commissioner

ATTEST:

Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE COMMISSION IN CASE NO. 8184 DATED September 11, 1981

The following rates and charges are prescribed for the customers in the area served by Henderson-Union Rural Electric Cooperative Corporation. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under the authority of this Commission prior to the date of this Order.

Monthly Rates:

Schedule A - Farm, Residential and Public Buildings*

Customer Charge per delivery point	$ 6.10
Energy Charge per KWH	.045555

Schedule B - Farm, Government or Commercial (50 KW or less)*

Customer Charge per delivery point	$10.90
Energy Charge per KWH	.049437

Schedule B-1 - Farm or Commercial (51 KVA to 501 KVA)*

Customer Charge per delivery point	$10.90
Demand Charge per KW	3.36
Energy Charge per KWH	.043694

Schedule LP-3 - Large Power (501 KVA to 2000 KVA)*

Customer Charge per delivery point	$17.20
Demand Charge per KW	6.25
Energy Charge per KWH:	
First 100,000 KWH	.031165
All Over 100,000 KWH	.025571

Schedule LP-4 - Large Power (Over 2000 KVA)*

Customer Charge per delivery point	$17.20
Demand Charge per KW	6.25
Energy Charge per KWH:	
First 100,000 KWH	.028886
All Over 100,000 KWH	.024920

Schedule D - Security Lamp*

Sodium or Mercury Vapor Lamp	
8,000 Lumen	$ 6.70
20,000 Lumen	9.75

Schedule SL - Street Lights*

8,000 Lumen	4.21
20,000 Lumen	7.98

Industrial Consumers Served Under Special Contract*

PEABODY COAL COMPANY

The monthly delivery point rate shall be:

(a) A demand charge of $6.25 per kilowatt of billing demand

(b) Plus an energy charge of 21.6358 mills per KWH consumed

THE ANACONDA COMPANY

(a) A demand charge of $6.25 per kilowatt of billing demand

(b) Plus an energy charge of 18.241 mills per KWH consumed

*The monthly kilowatt hour usage shall be subject to plus or minus an adjustment per KWH determined in accordance with the "Fuel Adjustment Clause."