

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

AMENDED APPLICATION OF FRIENDLY UTILITIES,)
INC., FOR AUTHORITY TO ACQUIRE AND TO)
OPERATE THE SEWAGE TREATMENT PLANT OWNED)
BY FUTURE FEDERAL SAVINGS AND LOAN ASSOCI-) CASE NO. 8459
ATION IN JEFFERSON COUNTY, KENTUCKY, AND)
FOR AUTHORITY TO INCUR THE NECESSARY DEBT)
TO ACQUIRE THE SAID SEWAGE TREATMENT PLANT)

O R D E R

On February 17, 1982, Friendly Utilities, Inc., ("Friendly") filed an application with the Commission seeking approval of the transfer of Friendly Hills East Sewer System ("Friendly Hills") from Future Federal Savings and Loan Association ("Future Federal") to Friendly pursuant to an assets purchase agreement entered into by Friendly and Future Federal dated December 30, 1981. This agreement was filed with the application as Exhibit 2.

A public hearing was held on May 19, 1982, at the Commission's offices in Frankfort, Kentucky, with all parties of record in attendance.

On June 11, 1982, Friendly filed an amended application with the Commission asking to include the approval of financing in the application. Friendly requested authorization to borrow \$160,000 to acquire the sewage treatment facilities of Friendly Hills at which time Friendly Hills will be liquidated and assumed by Friendly.

COMMENTARY

Friendly Hills is located in Jefferson County, Kentucky, and consists of a treatment plant and its adjacent collection system. The plant serves 244 customers and has a treatment capacity of 130,000 gallons per day.

Friendly received its Articles of Incorporation on November 26, 1981, with Carroll F. Cogan being sole stockholder and president.

FINDINGS IN THIS MATTER

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

1. Friendly is ready, willing and able to purchase, operate and provide adequate and reliable service to the customers presently served by Friendly Hills. Furthermore, Future Federal is ready and willing and desires to sell, inasmuch as it wishes to divest itself of the ownership and operation of this sewage treatment system.

2. The quality of service to the present customers of Friendly Hills will not suffer in that Andriot-Davidson Service Company, Inc., which has knowledge and experience in the operation and maintenance of sewage treatment facilities, will be employed to operate the system. Furthermore, Andriot-Davidson Service Company, Inc., is familiar with the construction and operation of this treatment plant.

3. The agreed-upon purchase price is \$160,000 which was determined through negotiations between Friendly and Future Federal.

4. Friendly has adopted the tariffs, rates, rules and regulations filed with the Commission by Friendly Hills for furnishing sanitary sewer service to its customers.

5. The third party trust agreement for this sewage treatment plant was entered into on February 10, 1982, between Friendly and Citizens Fidelity Bank and Trust Company, a Louisville, Kentucky, banking corporation. This agreement was filed with the application as Exhibit 3.

6. Friendly has filed with the Commission its Articles of Incorporation and Certificate of Incorporation as well as the bylaws adopted by its board of directors.

7. Friendly should maintain its books of account in accordance with the Uniform System of Accounts for Sewer Utilities prescribed by this Commission. Accounting for an acquisition includes:

- A. Recording the utility plant acquired at its original cost to the person first devoting it to public service, estimated if not known, in the appropriate utility plant in service accounts;
- B. Crediting the requirements for accumulated provision for depreciation and amortization applicable to the original cost of the properties acquired to the appropriate account for accumulated provision for depreciation and amortization;
- C. Transferring the cost of any nonutility property to Account 121, Nonutility Property;
- D. Crediting contributions in aid of construction to Account 271, Contributions In Aid of Construction; and

E. Including in Account 108, Utility Plant Acquisition Adjustment, any difference between the purchase price and the original cost of the utility plant and nonutility property less the amounts credited to accumulated depreciation and amortization reserves and contributions in aid of construction.

8. While legal and proper for general accounting purposes, this acquisition transaction, if not at "book value," can either increase or decrease the debt and/or equity on the utility's books. In this case the purchase price is less than net book value, therefore a "bargain purchase" has occurred. The negative acquisition adjustment that has resulted will not increase the plant value for rate-making purposes. It is the Commission's opinion that a bargain purchase is in effect a contribution and should be passed on to a utility's ratepayers. Also, the allowable interest charges should be computed using the weighted average cost of debt.

9. Friendly requested authorization to borrow \$160,000 from Future Federal. The financing is in the form of two separate notes. Note A, which is included in the application as Exhibit B, is for the principal sum of \$105,000 and for a term of 24 years. The initial interest rate is 13 percent and will be applicable for the first 3 years of the loan. After these 3 years the change in the interest rate will occur every 36 months and will be based on the prime lending rates established by First National Bank of Louisville.

Note B, which is included in the application as Exhibit C, is for the principal sum of \$55,000 and for a term of 36 years.

There are no interest charges for the first 24 years of the note. On January 1, 2006, the interest rate on the unpaid principal balance will be based on the changes in the prime lending rate established by First National Bank of Louisville. The interest rate on this note will be reestablished every 36 months in the same manner as originally established.

Clause 2 (b) of Note B states that if any additional customers, above the 244 that are now being served, are acquired by the utility during the term of this note the aid to construction fee for each new customer shall be paid by Friendly to Future Federal. The minimum fee shall be \$1,000 per customer with the exception of Lots 13 and 14, Friendly Hills Subdivision, for which the minimum fee shall be \$750 each. After Future Federal has received \$80,000 in these fees, then Friendly shall pay to Future Federal only one-half of the minimum aid to construction fee for each additional customer. Payments received pursuant to this clause shall be applied first to the principal of Note B. Any payments received in excess of \$55,000 shall constitute additional consideration for the extension of this loan.

The financing of \$160,000 by Future Federal to Friendly for the purchase of the sewage treatment facilities should be approved.

10. Carroll F. Cogan, president of Friendly, testified that following consummation of the proposed acquisition, the operating costs of Friendly Hills will be reduced because of

economies of scale inherent in operation and ownership of a number of sewer utilities under this Commission's jurisdiction. (1)

11. The Commission will review Friendly's financial statements to be filed as a part of its Annual Report for 1982 to determine the appropriateness of existing customer rates at that time.

12. Should operating expenses not be reduced as noted in finding number 11, the Commission will upon its own motion institute a formal investigation of Friendly's rates and operations.

13. The transfer of the assets of Friendly Hills should be approved.

ORDERS IN THIS MATTER

The Commission, on the basis of the evidence of record and the findings herein set forth:

HEREBY ORDERS that the transfer of Friendly Hills from its owner, Future Federal, to Friendly be and it hereby is approved.

IT IS FURTHER ORDERED that the financing of funds of \$160,000 as described in finding number 9 be and it hereby is approved.

IT IS FURTHER ORDERED that in future rate cases before the Commission allowable interest charges shall be determined as set out in finding number 8.

IT IS FURTHER ORDERED that Friendly shall adopt the existing rates, rules and regulations filed with and approved by the Commission for Friendly Hills.

(1) Transcript of Evidence, May 19, 1982, page 32.

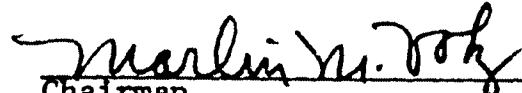
IT IS FURTHER ORDERED that Friendly shall file with this Commission within 30 days from the date of this Order its original tariff sheets setting forth rates, rules and regulations as required by KRS 278.160.

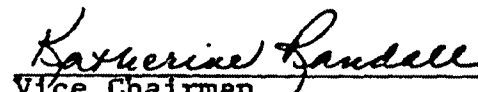
IT IS FURTHER ORDERED that Friendly shall file with this Commission within 30 days from the date of this Order the balance sheets of Friendly Hills and Friendly at the date of the transfer, the final journal entries required to consummate the transfer and the resulting balance sheet subsequent to the assumption of Friendly Hills by Friendly.

Nothing herein contained shall be deemed a warranty or finding of value of securities or financing authorized herein on the part of the Commonwealth of Kentucky or any agency thereof.

Done at Frankfort, Kentucky, this 11th day of August, 1982.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Secretary