

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of

THE FILING OF A GENERAL RATE)
INCREASE BY PRIMROSE PLACE) CASE NO. 8570
TREATMENT PLANT, INC.)

O R D E R

On July 21, 1982, Primrose Place Treatment Plant, Inc., ("Primrose") filed its application with this Commission to increase its rate pursuant to 807 KAR 5:076, Alternative Rate Adjustment Procedure for Small Utilities ("ARF"). Primrose stated in its application that the proposed rate would produce additional revenue of \$6,336 annually, an increase of 87 percent. The Commission has determined that, based upon 101 residential equivalents at the end of the test period, the proposed rate would produce additional revenue of \$9,696 annually, an increase of 133 percent. Based on the determination herein, the revenues of Primrose will increase by \$4,894 annually, an increase of 67 percent.

A hearing was not requested in this matter and in accordance with the provision of the ARF, no hearing was conducted. Therefore, the decision of the Commission is based on information contained in the application, written submissions, annual reports and other documents on file in the Commission's offices.

COMMENTARY

Primrose is a privately-owned sewage treatment system organized and existing under the laws of the Commonwealth of Kentucky, and serving approximately 66 customers in McCracken County.

TEST PERIOD

The Commission has adopted the 12-month period ending May 31, 1982, as the test period for determining the reasonableness of the proposed rates. In utilizing the historical test period, the Commission has given full consideration to known and measurable changes found reasonable.

REVENUES AND EXPENSES

The ARF was established to provide a simplified and less expensive method for small utilities to apply for rate increases with the Commission. Therefore, the financial data from the 1981 Annual Report is used as the basis for determining the revenue requirements. Primrose proposed several adjustments to its test period revenues and expenses. The Commission is of the opinion that the proposed adjustments are generally proper and acceptable for rate-making purposes with certain modifications. In addition the Commission has made several adjustments to Primrose's test period operating statement to reflect actual and anticipated operating conditions.

Operating Revenue

The actual operating statement of Primrose for the test period reflected operating revenue of \$7,500. In response to

item two of the request for information dated November 3, 1982, Primrose indicated that it had included in the test year operating revenues based on cash receipts which included billings for periods outside the test period. Therefore, the Commission has reduced operating revenues by \$228 to reflect the normalized annual revenue based on 101 monthly bills.

Maintenance, Supplies, and Insurance Expense

Primrose proposed pro forma adjustments to its maintenance, supplies, and insurance expense accounts. In each instance the adjustment was based upon Primrose's estimate of the future expense in each account. In response to an information request dated August 27, 1982, Primrose could offer no evidence in support of these adjustments. The Commission is of the opinion that adjustments of this nature are speculative and do not reasonably project the level of expense that may be incurred in the future. The Commission finds that those adjustments based upon estimates are not sufficiently known and measurable and has disallowed them in accordance with its previous policy.

Miscellaneous Expense

Primrose proposed to reduce its expenses to exclude \$460 charged to miscellaneous expense during the test year. Primrose offered no explanation in support of excluding this expense in its entirety. However, upon an analysis of the expenses comprising this account, the Commission finds that \$384 was for the purchase of valves and pumps which should be capitalized in

accordance with the Uniform System of Accounts. Therefore, the Commission has reduced miscellaneous expense by \$384 for rate-making purposes.

Depreciation Expense

As mentioned in the preceding adjustment, the Commission has capitalized an expenditure of \$384 inadvertently charged to miscellaneous expense. This expenditure represents valves purchased at an installed price of \$264 and diffusers purchased at an installed price of \$120. The Commission has determined that the valves should be depreciated over an estimated useful life of 10 years and the diffusers should be depreciated over an estimated useful life of 3 years resulting in total depreciation of \$64 annually. This adjustment will increase Primrose's depreciation expense by \$64.

Electric Expense

The Commission has adjusted test year electric expense to reflect the current rates in effect from Primrose's electric supplier, Paducah Power System. In determining the pro forma electric expense, the Commission has applied the current rates to the actual KWH used by Primrose during the test year. This results in an adjusted electric expense of \$2,360.

Income Taxes

Although Primrose did not propose an adjustment for federal and state income taxes, the Commission has included a provision of \$338, based on the level of net income allowed herein and the applicable federal and state tax rates.

The Commission finds that Primrose's adjusted test period operations are as follows:

	<u>Actual Test Period</u>	<u>Pro Forma Adjustments</u>	<u>Adjusted Test Period</u>
Operating Revenues	\$ 7,500	\$ (228)	\$ 7,272
Operating Expenses	<u>10,332</u>	<u>575</u>	<u>10,907</u>
Net Income	<u>\$ (2,832)</u>	<u>\$ (803)</u>	<u>\$ (3,635)</u>

REVENUE REQUIREMENTS

Primrose requested operating revenues sufficient to produce a 7 percent return on the value of plant in service at May 31, 1981. In determining the level of investment in plant devoted to public use for rate-making purposes, a well established formula is used by this Commission. The rate of return is applied to the net investment rate base which is determined by adding materials and supplies, prepayments and working capital to the total utility plant in service and deducting accumulated depreciation and contributions in aid of construction. In this case the Commission finds that a 7 percent return on a justifiable rate base would result in insufficient revenue for Primrose to maintain its financial integrity.

The Commission has consistently used the operating ratio method to determine the revenue requirements of sewer utilities because of certain problems involved in arriving at a legitimate rate base. In this case the Commission finds that an operating ratio⁽¹⁾ of 88 percent is fair, just and reasonable and will allow

(1) Operating Ratio =
$$\frac{\text{Operating Expenses} + \text{Depreciation} + \text{Taxes}}{\text{Gross Revenue}}$$

Primrose to pay its operating expenses, service its debt, and provide a reasonable return to its owners. Therefore, the Commission finds that Primrose is entitled to increase its rate to produce total revenues of \$12,394 which will require an increase of \$4,894 annually.

OTHER ISSUES

During the course of its examination of this request for rate relief, the Commission has learned that Primrose has filed this case and its annual reports of previous years on a fiscal year basis rather than the calendar year basis required by the Uniform System of Accounts and Commission regulations. The Commission hereby notifies Primrose that it should file its annual reports beginning with the report covering operations for the 12-month period ending December 31, 1982, on a calendar year basis as required by 807 KAR 5:066.

SUMMARY

The Commission, after consideration of the evidence of record, finds that:

- (1) The rate in Appendix A will produce gross annual operating revenue of \$12,394 and is the fair, just and reasonable rate to be charged in that it will allow Primrose to pay its operating expenses and provide a reasonable surplus for equity growth.
- (2) The rate proposed by Primrose should be denied.

(3) Primrose has not filed its annual reports with the Commission on the calendar year basis as required by the Uniform System of Accounts.

IT IS THEREFORE ORDERED that the proposed rate in Primrose's application be and it hereby is denied.

IT IS FURTHER ORDERED that the rate in Appendix A be and it hereby is approved for sewer service rendered by Primrose on and after the date of this Order.

IT IS FURTHER ORDERED that within 30 days of the date of this Order, Primrose shall file its revised tariff sheets setting forth the rate approved herein.


IT IS FURTHER ORDERED that Primrose shall file its 1982 and all subsequent annual reports on the calendar year basis.

Done at Frankfort, Kentucky, this 6th day of January, 1983.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE
COMMISSION IN CASE NO. 8570 DATED January
6, 1983.

The following rate is prescribed for all customers served by Primrose Place Treatment Plant, Inc. All rates and charges not specifically mentioned herein shall remain the same as those in effect prior to the date of this Order.

RATES: Monthly

Customer Category

Single Family Residential

\$10.23 per residence