COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

THE APPLICATION OF WILLIAM DOHR-)
MAN, INC. - THORNHILL TREATMENT)
PLANT FOR AN ADJUSTMENT OF RATES) CASE NO. 9060
PURSUANT TO THE ALTERNATIVE RATE)
FILING PROCEDURE FOR SMALL)
UTILITIES)

O R D E R

On May 18, 1984, William Dohrman, Inc. - Thornhill Treatment Plant ("Thornhill") filed an application with the Commission to increase its sewer rate pursuant to 807 KAR 5:076, Alernative Rate Adjustment Procedure for Small Utilities ("ARF"). This regulation permits utilities with 400 or fewer customers or $200,000 or less gross annual revenues to use the alternative filing method to minimize the necessity for formal hearings, to reduce filing requirements and to shorten the time between the application and the Commission's final Order. This procedure minimizes rate case expenses to the utility and, therefore, results in lower rates to the ratepayers.

Thornhill's proposed rates would produce additional revenue of approximately $16,655 annually, an increase of 47.4 percent. Based on the determination herein, the revenues of Thornhill will increase by $6,575 annually, an increase of 18.7 percent.

A hearing was not requested in this matter, and in accordance with the provisions of the ARF, no hearing was conducted.

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 offices.

COMMENTARY

Thornhill is a privately-owned sewage treatment plant and serves approximately 266 residential customers, one commercial customer, and one public authority in Jefferson County, Kentucky.

TEST PERIOD

The Commission has adopted the 12-month period ended December 31, 1983, 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

For the test period Thornhill had a net operating loss from sewage operations of $5,890. Thornhill proposed several pro forma adjustments to revenues and expenses to reflect more current and anticipated operating conditions. The Commission is of the opinion that the proposed adjustments are generally proper and acceptable for rate-making purposes with the following modifications:

Management Fee

Thornhill proposed to increase the test-period management fee of $1,380 by $1,210, an increase of 87.7 percent. Thornhill's basis for the adjustment is that the management fee should be 5 percent of annual revenues collected which is the standard practice in the real estate industry.

The Commission has determined that this "rule of thumb" for the real estate industry is not relevant to this situation. Furthermore, Thornhill did not provide, in response to an information request,[1] the additional services that would be provided that might require an increase in the management fee. Therefore, the proposed adjustment has not been included herein and the actual test-year expense of $1,380 has been included for rate-making purposes.

Billing Costs

Thornhill proposed to increase test-period billing costs of $147 by $166 in order to reflect current billing costs. In its original application, Thornhill stated that the pro forma increase was based on the Louisville Water Company ("Louisville Water") charge to perform billing functions. However, Thornhill's billing is done internally by office personnel. Therefore, as no evidence was provided of an actual increase in billing costs, the Commission has rejected this adjustment in accordance with its policy of accepting only known and measurable increases in test period expenses, and the test year expense of $147 has been included for rate-making purposes.

Water Expense

Thornhill proposed an adjustment to test-period water expense in the amount of $239. Thornhill's calculation of the adjustment included 5 percent sales tax, whereas copies of

1 Response to Commission's Information Request dated June 27, 1984, Item No. 15.

invoices show that no sales tax is paid on bills from Louisville Water. Applying Louisville Water's rates as of January 1, 1984, to test-year consumption results in an increase of $119 which has been included as an adjustment for rate-making purposes.

Electricity Expense

Thornhill proposed an adjustment to test-period electricity expense in the amount of $282. However, the projected increase was not calculated based on the rate increase granted to Louisville Gas and Electric Company in May, 1984. The Commission has determined that the adjustment should be $924 and that amount has been allowed for rate-making purposes.

Maintenance of Treatment and Disposal Plant Expenses

Thornhill reported test-period maintenance of treatment and disposal plant expenses of $5,348. However, the Commission has determined that several items that were expensed during the test year should have been capitalized. All of the items should be added to plant Account No. 373--Treatment and Disposal Equipment. These items, with invoice date(s) in parentheses, are:

1. 3-inch gate valve (February 9, 1983), $174 [including sales tax];
2. diffusers (May 19, 1983), $856;
3. 8-inch comminutor (June 23, 1983), $1,391;
4. steel cutter drum (September 29, 1983, and October 15, 1983), $942;
5. vent motor (September 13, 1983), $123; and
6. time clock (September 13, 1983), $186.

The total amount of these items which should be capitalized is $3,672. Therefore, the Commission has reduced maintenance of treatment and disposal plant expense by $3,672 which results in an adjusted expense of $1,676 for rate-making purposes. The Commission has determined that the gate valve should be depreciated over a period of 30 years, while the other items mentioned above should be depreciated over 15 years, with the straight-line method being applied in all instances.

Depreciation Expense

Thornhill reported test-period depreciation expense of $5,976. A depreciation schedule submitted by Thornhill revealed that some items of plant were depreciated by the declining-balance method, whereas the Commission requires straight-line depreciation for rate-making purposes. The Commission has determined that the undepreciated balance of the aforesaid items at the beginning of the test period should be depreciated by the straight-line method over the remaining useful lives. The plant truck equipment, equipment and installation, and fence should be depreciated on a straight-line basis over 10 years, the machinery over 4 years, and the building over 16 years.

Since the difference between the amount of depreciation taken by Thornhill during the test period and that resulting from the method described above is immaterial, no adjustment has been made on the basis of depreciation method. However, it is an established policy of the Commission to disallow, for rate-making purposes, depreciation associated with contributed property. According to the 1983 Annual Report, gross utility plant in service at the end of the test period amounted to $192,113. Contributions in aid of construction totaled $147,351 at the end of the test year. Thus, depreciation on contributed property comes to $4,584.

The Commission has determined that an additional adjustment should be made to depreciation expense. As mentioned previously in the section on maintenance of treatment and disposal plant expenses, items totaling $3,762 should have been capitalized rather than expensed. Test-year depreciation expense should be increased by $239 to reflect depreciation on these items that should be added to plant Account No. 373--Treatment and Disposal Equipment. The net effect of the two adjustments is to decrease the test-period depreciation expense by $4,345. Therefore, a depreciation expense of $1,631 has been allowed for rate-making purposes.

After consideration of the aforementioned adjustments, the Commission finds Thornhill's test period operations to be as follows:

	Actual Test Period	Pro Forma Adjustments	Adjusted Test Period
Operating Revenues	$35,148	-0-	$35,148
Operating Expenses	41,038	$<4,322>	36,716
Net Income <Loss>	$<5,890>	$ 4,322	$<1,568>

REVENUE REQUIREMENTS

The Commission is of the opinion that the adjusted test-period operating loss is clearly unjust and unreasonable. Thornhill based its requested increase on an operating ratio methodology and requested revenue sufficient to produce a ratio of .88.

The Commission is of the opinion that the operating ratio[2] is a fair, just and reasonable method for determining revenue requirements in this case and finds that an operating ratio of 88 percent will allow Thornhill to pay its operating expenses and provide a reasonable return to its owners. Therefore, the Commission finds that Thornhill is entitled to an increase in annual revenue of $6,575.

FINDINGS AND ORDERS

1. The rates in Appendix A are the fair, just and reasonable rates for Thornhill and will produce gross annual revenue of approximately $41,723.

2. The rates proposed by Thornhill would produce revenue in excess of that found reasonable herein and should be denied upon application of KRS 278.030.

IT IS THEREFORE ORDERED that the rates in Appendix A be and they hereby are approved for service rendered by Thornhill on and after the date of this Order.

IT IS FURTHER ORDERED that the rates proposed by Thornhill be and they hereby are denied.

IT IS FURTHER ORDERED that within 30 days from the date of this Order, Thornhill shall file with the Commission its revised tariff sheets setting out the rates approved herein.

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2 $\text{Operating Ratio} = \dfrac{\text{Operating Expenses}}{\text{Gross Revenue}}$

Done at Frankfort, Kentucky, this 26th day of September, 1984.

PUBLIC SERVICE COMMISSION

Chairman

Vice Chairman

Commissioner

ATTEST:

Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE COMMISSION IN CASE NO. 9060 DATED 9/26/84

The following rates are prescribed for the customers in the area served by William Dohrman, Inc. - Thornhill Treatment Plant located in Jefferson County, Kentucky. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of the Commission prior to the effective date of this Order.

RATES: Monthly	
Single Family Residential	$13.62
Multi-Family	8.94
All Other	
(Per Residential Equivalent)	16.07