

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

NOTICE OF PUBLIC GAS COMPANY, INC.,)
OF GENERAL RATE ADJUSTMENT EFFECTIVE) CASE NO. 9565
MAY 12, 1986)

O R D E R

On November 14, 1986, the Commission issued an Order granting Public Gas Company, Inc., ("Public") a rehearing on two issues adjudicated in the October 10, 1986, Order authorizing an adjustment in gas rates. The issues pending on rehearing are a secretarial salary and rent expense.

A hearing was held on February 18, 1987, at the Commission's offices in Frankfort, Kentucky. There were no intervenors at the hearing.

Secretarial Salary

In its Order of October 10, 1986, the Commission disallowed the inclusion of a secretarial salary as part of the total level of wages and salaries allowed for rate-making purposes. For a utility with expenses net of gas purchases of \$140,971 and with annual revenues of approximately \$450,000, the total wages and salaries of \$36,600 were considered reasonable given the fact that the general manager spent 70 percent of his time on administrative duties, that Public hired an outside consulting firm to perform accounting and bookkeeping functions, and a field maintenance person was also employed. The \$36,600 does not include the

charges for the outside consulting firm, which totaled \$7,200 for the test year. Upon rehearing, Public has provided detailed information regarding the secretarial salary and the job duties of the secretary, general manager, and outside consulting firm.

In Public's petition for rehearing, it was stated that, "The claimed salary amount [for the secretary] was \$14,304 plus other costs."¹ The record reflects that the test year total for salaries and wages was \$56,487 and the only proposed adjustment was to recognize a \$4,235 reimbursement from the Pan Bowl Production Gas Company ("Pan Bowl"). Public did not reduce test year expenses to reflect the termination of an arrangement with the PATS Service Company which made up \$21,773 of the reported salary expense, nor did Public attempt to adjust the partial year salaries paid to its own employees to an annual basis. In summary, Public had made no claim for a secretarial salary of \$14,304 prior to the petition for rehearing.

Public filed detailed listings of the assigned job duties for its secretary, general manager, and the outside consulting firm.² While the duties listed for the secretary are quite extensive, there appears to be some overlap with the services provided by the outside consulting firm, especially with the accounting and book-keeping functions. For example, the outside consulting firm is to provide the accounting and bookkeeping duties of Public. Edmund

¹ Public's Petition for Rehearing, filed October 28, 1986, page 1.

² Response to the Commission's Order Granting Rehearing, filed December 29, 1986, Item Nos. 1, 3, and 4.

Vachon, the President of Public, stated at the rehearing that this function of the consulting firm could not be performed by Public's secretary because she was not a bookkeeper.³ Yet the secretarial duties were said to include the initial preparation of quarterly tax withholding filings and deposits, billing, collecting and preparation of payroll.

In all the responses Public has filed since rehearing was granted, its recurring theme has been that it needs a full-time secretary.⁴ Yet, for the test year, and 11 months in the subsequent year, Public shared its secretary with Pan Bowl. While Public states that the workload was split 80 percent Public and 20 percent Pan Bowl, Public was reimbursed at a rate of 50 percent. Mr. Vachon stated at the rehearing that because of the arrangement, Pan Bowl was in effect subsidizing the secretarial expense of Public.⁵ No documentation of this subsidization was provided in these proceedings.

The Commission acknowledges the objections of Public to the introduction of evidence regarding the outside consulting firm. However, the information is necessary in order to assess the purported need for the secretary. Further, based on the available evidence, Public's relationship with its consulting firm, Armadas, Inc., ("Armadas") is a less-than-arms-length transaction because of the involvement of Mr. Vachon in both businesses. Where less-

³ Rehearing Transcript, February 18, 1987, page 17.

⁴ Ibid., pages 6-7, 16.

⁵ Ibid., pages 12-13.

than-arms-length transactions exist it is incumbent upon the Commission to consider whether said transactions are reasonable.

The Commission has noted that what was initially portrayed as a part-time secretary position evolved through testimony and various exhibits into a secretary/receptionist position to an office cashier and billing clerk position with public relations duties. The conflicting testimony has done nothing but compound the issues in the case.

Based on the foregoing, the Commission finds that Public has not provided any persuasive evidence that the \$36,600 allowed in the October 10, 1986, Order was not a reasonable level of salary and wage expense based on the personnel needs of Public. The evidence submitted by Public which has been confusing and contradictory does not justify the additional amount required for a full-time secretary. Public states that the claimed salary for a secretary was \$14,304; however, no such claim was advanced until the filing of a petition for rehearing. Public states that it needs a full-time secretary, yet during the test year and the majority of the subsequent year, Public shared a secretary with Pan Bowl and the expense was subsidized by Pan Bowl. The Commission, in determining from the record what are reasonable salary expenses for rate-making purposes, is not attempting to dictate the hiring practices or organizational structure of Public. However, the Commission finds that the salaries of \$36,600, when combined with the consultant fees allowed in the original Order, are adequate. Therefore, the finding regarding this issue in the October 10, 1986, Order should be affirmed.

Rent Expense

In its Order of October 10, 1986, the Commission disallowed an increase to the rent expense of \$3,950. Public had sought the increase based upon the annualization of its test-year-end rent expense of \$750 per month, or \$9,000, over its actual test year expense of \$5,050. The rent expense at the beginning of the test year was \$200 per month. Because of the substantial increase in the rent expense and the longstanding business connection between its landlord and Public, the burden of proof that the price charged is fair, just and reasonable rests solely with Public. Upon rehearing, Public has provided additional information concerning its rental situation.

In Public's petition for rehearing, it is stated that, "The Commission Order, at page 10, disallowed \$5,050 of the claimed \$9,000 rent expense."⁶ In actuality, the October 10, 1986, Order allowed \$5,050 rent expense and disallowed \$3,950.

Public filed information detailing the office space rented, its uses, and an estimate of the space it believes the utility requires. While Public rented 9,600 square feet, it has estimated that it requires 2,500 square feet.⁷ Thus, Public is renting 7,100 square feet that it does not need; in other words, it only requires the use of approximately 26 percent of the area currently rented. The claimed annual rent of the 9,600 square feet was

⁶ Public's Petition for Rehearing, filed October 28, 1986, page 1.

⁷ Response to Commission's Order granting rehearing, filed December 29, 1986, Rent Expense, Item No. 1.

\$9,000, 94 cents per square foot per year. Applying that rate to what Public has stated as the space it requires, the annual cost would be \$2,350.⁸

In the petition for rehearing, Public challenges several statements made in the October 10, 1986, Order as being speculative and based upon suspicion. The petition further states, "...Mr. Vachon testified that his only connection with the owners of Panbowl was that Public purchased its gas supply from Panbowl...."⁹ In Affidavit No. 2 to the petition for rehearing, Mr. Vachon states "...any and all dealings between Public and Panbowl are at arms length...."¹⁰ At the September 18, 1986, hearing, Mr. Vachon stated that Caesar McCoun was the landlord of the building Public rented space in; Edsel McCoun, the son of Caesar McCoun, was associated with Pan Bowl; and the previous owner of Public was Caesar McCoun.¹¹

In fairness to Public, these statements were explored in the rehearing of February 18, 1987. At the rehearing, Mr. Vachon testified that Caesar McCoun was Public's landlord during the test year and is currently the landlord; and Mr. Vachon had purchased Public from Edsel McCoun.¹² According to information on file with

⁸ 2,500 square feet X \$.94 = \$2,350

⁹ Public's Petition for Rehearing, filed October 28, 1986, page 3.

¹⁰ Ibid., Affidavit No. 2 of Ed Vachon.

¹¹ Hearing Transcript, September 18, 1986, pages 26-27, 29.

¹² Rehearing Transcript, February 18, 1987, pages 23, 29.

the Commission, Edsel McCoun was the manager of Pan Bowl during the test year and for the majority of the subsequent year. Mr. Vachon has also testified that the other occupant of the building Public rented during the test year was Pan Bowl.¹³

Throughout these proceedings, Public has contended that the increase in the monthly rent expense from \$200 to \$750 per month was justified because it allowed Caesar McCoun a fair return on his rental property. Mr. McCoun had charged Public only a token amount for rent during his ownership of Public, but after Mr. Vachon purchased the utility, Mr. McCoun wished to receive fair value for the space leased.¹⁴ However, Mr. Vachon testified at the rehearing that during the test year, while Public was sharing the building with Pan Bowl, Public's rent was a fixed amount and not based on an allocation of expense with Pan Bowl.¹⁵ If a fair return on the rental property was a concern of Mr. McCoun, then an allocation of the rental expense among the tenants would have been expected.

The Commission is concerned that Public has failed to secure a written lease agreement for its office space. Mr. Vachon has testified that no written agreement existed at the time he purchased Public, nor did one exist during the test year, nor does

¹³ Ibid., page 28.

¹⁴ Hearing Transcript, September 18, 1986, page 29.

¹⁵ Rehearing Transcript, February 18, 1987, page 28.

a written agreement exist currently.¹⁶ It is not a good business practice to enter into a lease arrangement without the benefit of a written agreement, regardless of the size of the lessee. The terms of a written lease for a business would normally include provisions to cover an early termination due to a move by the lessee or the sale of the rental property by the lessor. By not securing a written lease agreement, Public has left itself susceptible to arbitrary increases in rent by its landlord. Public's customers are also affected because they must pay higher gas bills to cover these increased rental expenses.

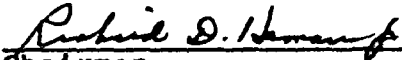
Based on the foregoing, the Commission finds that Public has not met its burden of proof that the rent charged was fair, just or reasonable. Public has been renting nearly three times the space it states it needs. Public has not provided any persuasive evidence as to why the Commission should consider the fair return on rented property for Public's landlord. Further, the Commission finds that Public's management should have secured a written lease agreement for the rented property. The Commission allowed a total rent expense of \$5,050 in its October 10, 1986, Order and finds no further adjustment should be made at this time. The October 10, 1986, finding regarding this issue is therefore affirmed.

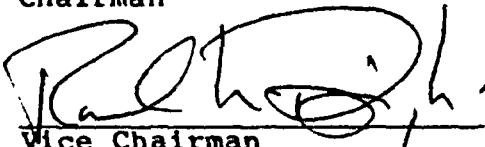
IT IS THEREFORE ORDERED that the findings and decisions of the Commission's Order dated October 10, 1986, are hereby affirmed in all aspects.

16 Ibid., page 29.

Done at Frankfort, Kentucky, this 9th day of April, 1987.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Executive Director