

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF DOE VALLEY UTILITIES,)
INC. FOR AN ADJUSTMENT OF WATER AND SEWER) CASE NO.
RATES PURSUANT TO THE ALTERNATIVE RATE) 93-263
FILING PROCEDURE FOR SMALL UTILITIES)

O R D E R

On July 26, 1993, Doe Valley Utilities, Inc. ("Doe Valley") filed its application for Commission approval of proposed increased water and sewer rates. Commission Staff, having performed a limited financial review of Doe Valley's operations, has prepared the attached Staff Report containing Staff's findings and recommendations regarding the proposed rates. All parties should review the report carefully and provide any written comments or requests for a hearing or informal conference no later than 15 days from the date of this Order.

IT IS THEREFORE ORDERED that all parties shall have no more than 15 days from the date of this Order to provide written comments regarding the attached Staff Report or requests for a hearing or informal conference. If no request for a hearing or informal conference is received, then this case will be submitted to the Commission for a decision.

Done at Frankfort, Kentucky, this 7th day of October, 1993.

PUBLIC SERVICE COMMISSION


For the Commission

ATTEST:


Executive Director

COMMONWEALTH OF KENTUCKY
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STAFF REPORT

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Public Utility Financial
Analyst
Water and Sewer Revenue
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Public Utility Rate
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STAFF REPORT

ON

DOE VALLEY UTILITIES, INC.

CASE NO. 93-263

A. Preface

On July 26, 1993, Doe Valley Utilities, Inc. ("Doe Valley") filed its application with the Kentucky Public Service Commission ("Commission") seeking approval to increase its tariffed water and sewer rates by \$25,234 and \$9,270 or 45 and 50 percent, respectively.

In order to evaluate the requested increase, the Commission Staff ("Staff") chose to perform a limited financial review of Doe Valley's operations for the test period, the twelve month period ending December 31, 1992. Jack Scott Lawless, of the Commission's Division of Financial Analysis began the review on August 19, 1993 at Doe Valley's office in Brandenburg, Kentucky. Brent Kirtley of the Commission's Division of Rates and Research performed a review of Doe Valley's reported revenues at the offices of the Commission.

The findings of the field review have been reduced to writing in this report. Mr. Kirtley is responsible for the sections related to operating revenues and rate design. The remaining sections of the report were prepared by Mr. Lawless. Based upon the findings of this report, Staff recommends that Doe Valley's water and sewer divisions be allowed to increase their normalized operating revenues by \$9,778 and \$3,181 or 17.58 and 12.78 percent, respectively.

Scope

The scope of the review was limited to obtaining information to determine whether test period operating revenues and expenses were

representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

During the course of the review, Doe Valley was advised that all proposed adjustments to test year expenses must be supported by some form of documentation and that all such adjustments must be known and measurable.

DOE VALLEY - WATER DIVISION

B. Analysis of Operating Revenues and Expenses

Operating Revenue

The Water Division reported test-year total operating revenue of \$55,629. Staff made no adjustments to revenue from rates or other operating revenue. Therefore, for the purpose of this report, normalized test-year operating revenue shall be considered to be \$55,629.

Operating Expenses

The Water Division reported test year operating expenses of \$119,452 which it proposed to increase by \$14,420. These adjustments were based on estimates of inflation and consumption of supplies. It is Staff's position that Doe Valley's adjustments are not known and measurable and should therefore be disallowed for rate-making purposes. Staff has also reduced test-year operating expenses by \$11,379 as detailed in Appendix C and discussed in the following sections of this report.

Salaries and Wages and FICA

The Water Division reported test year Salaries and Wages of \$50,574. Staff has increased this amount by \$1,389 to reflect the pro forma payroll expense of \$51,963. Staff's pro forma payroll was determined by utilizing the most current wage rates paid to the employees and should therefore be accepted for rate-making purposes. Staff has increased taxes other than income taxes by \$106 to reflect the increase in FICA as a result of the increase in test year salaries and wages.

Purchased Water

The Water Division reported test year purchased water expense of \$5,712. This account includes amounts paid to an affiliated entity for the purchase of raw water at a price of \$.20 per one thousand gallons. That entity also sells raw water to the Olin Corporation for \$.06 per thousand gallons. This pricing discrepancy was not justified or explained to Staff during its field review. Staff is of the opinion that the customers of the Water Division should not have to pay more for raw water than an unaffiliated customer unless it is justifiable. Therefore, Staff has reduced test year purchased water by \$3,998¹ to reflect the same price paid by the Olin Corporation of \$.06 per thousand gallons.

¹ Gallons Purchased (000) omitted	28,558
Times: Rate per 1,000 gallons	<u>\$.06</u>
Pro Forma Expense	\$ 1,714
Less: Test Year Expense	<u>(5,712)</u>
Adjustment	<u>\$ (3,998)</u>

Materials and Supplies

Staff has adjusted materials and supplies to reflect the capitalization of meter installation supplies that were purchased within the test year. The total cost was \$3,571 which was eliminated from test year operation and maintenance expenses but will be recovered by an -adjustment to test year depreciation expenses.

Miscellaneous

During the review, Staff discovered that expenses totaling \$1,040 were erroneously omitted from the income statement as stated in Doe Valley's annual report. Staff has included these omissions by adjusting the miscellaneous account by \$1,040.

Depreciation

The Water Division reported test year depreciation expense of \$17,617. This amount was calculated using a 20 year depreciable life for the Water Division's pre-1989 Utility Plant in Service. After consulting with the Commission's Division of Engineering, Staff has determined that a 40 year depreciable life would be more appropriate and would be more comparable with the depreciation rates used by other utilities. Therefore, Staff recommends that test year depreciation be reduced by \$7,242 in order to reflect a 40 year depreciable life.

Staff has also increased test year depreciation expense by \$897² to allow the Water Division to recover the cost of the meter installations and a post-test period purchase of a pump.

B. Revenue Requirements Determination

An approach frequently used by this Commission to determine revenue requirements for small, privately owned utilities is an 88 percent operating ratio. Staff recommends the use of this approach in determining the Water Division's revenue requirements.

When using the approach recommended by Staff, the Water Division's revenue requirements are \$122,810³. Staff recommends that the Water Division be allowed to increase its normalized operating revenue by \$9,778⁴.

C. Rate Design

In its application, the Water Division filed a schedule of present and proposed rates that did not include any changes in its rate design.

²	Test year expenditure	\$ 3,571
	Post-test period additions	<u>2,710</u>
	Total	\$ 6,281
	Divide by: Depreciable life	<u>7</u>
	Adjustment	<u>\$ 897</u>
³	Pro forma operating expenses	\$ 108,073
	Divide by: Operating Ratio	<u>.88</u>
	Revenue Requirement	<u>\$ 122,810</u>
⁴	Revenue requirement	\$122,810
	Less: Operating revenue	55,629
	Non-operating revenue	<u>57,403</u>
	Required increase in revenues	<u>\$ 9,778</u>

Staff agrees that the current rate structure should not be altered. The recommended rates will generate operating revenue from water sales of \$65,407. This amount plus the amount collected for availability fees of \$57,403 will equal the total revenue requirement of \$122,810. Therefore, Staff recommends the rates in Appendix A be approved for water service.

DOE VALLEY - SEWER DIVISION

A. Analysis of Operating Revenues and Expenses

Operating Revenues

The Sewer Division reported test-year total operating revenue of \$24,888. Staff made no adjustments to revenue from rates or other operating revenue. Therefore, for the purpose of this report, normalized test-year operating revenue shall be considered to be \$24,888.

Operating Expenses

The Sewer Division reported test year operating expenses of \$74,026 which it proposed to increase by \$2,869. These adjustments were based on estimates of inflation and consumption of supplies. It is Staff's position that Doe Valley's adjustments are not known and measurable and should therefore be disallowed for rate-making purposes. Staff has also reduced test period operating expenses in the amount of \$10,036 as detailed in Appendix D and discussed in the following sections of this report.

Salaries and Wages and FICA

The Sewer Division reported test year Salaries and Wages of \$21,281. Staff has increased this amount by \$591 to reflect the pro forma payroll expense of \$21,872. Staff's pro forma payroll was determined by utilizing the most current wage rates paid to the employees and should therefore be accepted for rate-making purposes. Staff has increased taxes other than income taxes by \$45 to reflect the increase in FICA as a result of the increase in test year salaries and wages.

Administrative and General

During the field review, Staff discovered that expenses totaling \$859 were erroneously omitted from the income statement as stated in Doe Valley's annual report. Staff has included these omissions by adjusting the administrative and general account by \$859.

Depreciation

The Sewer Division reported test year depreciation expense of \$24,935. This amount was calculated using a 20 year depreciable life for the Sewer Division's pre-1989 Utility Plant in Service. After consulting with the Commission's Division of Engineering, Staff has determined that a 40 year depreciable life would be more appropriate and would be more comparable with the depreciation rates use by other utilities. Therefore, Staff recommends that test year depreciation be reduced by \$11,531 in order to reflect a 40 year depreciable life.

B. Revenue Requirements Determination

An approach frequently used by this Commission to determine revenue requirements for small, privately owned utilities is an 88 percent operating ratio. Staff recommends the use of this approach in determining the Sewer Division's revenue requirements.

When using the approach recommended by Staff, the Sewer Division's revenue requirements are \$72,716⁵. Staff recommends that the Sewer Division be allowed to increase its normalized operating revenue by \$3,181⁶.

C. Rate Design

In its application, the Sewer Division filed a schedule of present and proposed rates that did not include any changes in its rate design. However, Staff recommends that the current rate design be altered to provide a flat-rate monthly charge for sewer service. The required revenue has been divided equally among the 353 sewer customers. The recommended rate will generate operating revenue from sales of \$28,069. This amount plus the amount collected for availability fees of \$44,647 will equal the total revenue requirement of \$72,716. Therefore, Staff recommends the rates in Appendix B be approved for sewer service.

⁵	Pro forma operating expenses	\$ 63,990
	Divide by: Operating Ratio	<u>.88</u>
	Revenue Requirement	<u>\$ 72,716</u>
⁶	Revenue requirement	\$ 72,717
	Less: Operating revenue	24,888
	Non-operating revenue	<u>44,647</u>
	Required increase in revenues	<u>\$ 3,181</u>

E. Signatures

Jack Scott Lawless, CPA
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Public Utility Financial
Analyst
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Brent Kirtley
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Research Division

APPENDIX A
TO STAFF REPORT CASE NO. 93-263

The Staff recommends the following rate be prescribed for customers of Doe Valley Utilities, Inc.

Schedule of Rates

First 3,000 gallons	\$9.25 Minimum Bill
Next 4,000 gallons	2.50 per 1,000 gallons
Over 7,000 gallons	2.30 per 1,000 gallons

APPENDIX B
TO STAFF REPORT CASE NO. 93-263

The Staff recommends the following rate be prescribed for customers of Doe Valley Sewer Division.

Schedule of Rates

Monthly Charge	\$6.65
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APPENDIX C
TO STAFF REPORT CASE 93-263

Doe Valley - Water Division
Statement of Adjusted Operations

	Test Year	Adjustments	Pro forma Present Rates
Operating Revenue			
Metered Sales	\$ 55,629		\$ 55,629

- Total Operating Revenue	55,629	0	55,629

Operating Expenses			
Operation and Maintenance			
Salaries and Wages	50,574	1,389	51,963
Employee Pensions/Benefits	2,896		2,896
Purchase Water	5,712	(3,998)	1,714
Purchase Power	7,653		7,653
Chemicals	4,683		4,683
Materials and Supplies	11,576	(3,571)	8,005
Contractual Services	2,215		2,215
Transportation Expense	1,106		1,106
Insurance	4,090		4,090
Miscellaneous	5,066	1,040	6,106

Total Operation and Maintenance	95,571	(5,140)	90,431

Depreciation	17,617	(7,242)	11,272
		897	11,272
Taxes Other Than Income Taxes	6,264	106	6,370

Total Operating Expenses	119,452	(11,379)	108,073

Net Operating Income	(63,823)	11,379	(52,444)

Other Non-Operating Revenue			
Availability Fees	57,403		57,403

Regulated Income	\$ (6,420)	\$ 11,379	\$ 4,959
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APPENDIX D
TO STAFF REPORT CASE 93-263

Doe Valley - Sewer Division
Statement of Adjusted Operations

	Test Year	Adjustments	Pro forma Present Rates
Operating Revenue			
Metered Sales	\$ 24,888		\$ 24,888

- Total Operating Revenue	24,888	0	24,888

Operating Expenses			
Operation and Maintenance	24,636	591	25,227
Customer Accounts	3,000		3,000
Administrative and General	18,039	859	18,898
Depreciation	24,935	(11,531)	13,404
Taxes Other Than Income Taxes	3,416	45	3,461

Total Operating Expenses	74,026	(10,036)	63,990

Net Operating Income	(49,138)	10,036	(39,102)

Other Non-Operating Revenue			
Availability Fees	44,647		44,647

Regulated Income	\$ (4,491)	\$ 10,036	\$ 5,545
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