COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF THELMA WASTE CONTROL, INC.)
FOR AN ADJUSTMENT OF RATES PURSUANT TO THE)
ALTERNATIVE RATE FILING PROCEDURE FOR) CASE NO. 95-236
SMALL UTILITIES)

O R D E R

On June 15, 1995, Thelma Waste Control, Inc. ("Thelma Waste") filed its application for Commission approval of proposed sewer rates. Commission Staff, having performed a limited financial review of Thelma Waste'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, this case will be submitted to the Commission for a decision.

Done at Frankfort, Kentucky, this 6th day of November, 1995.

ATTEST:

Don Mills
Executive Director

PUBLIC SERVICE COMMISSION

Robert M. Davis
For the Commission

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF THELMA WASTE CONTROL, INC. FOR A RATE ADJUSTMENT PURSUANT TO THE ALTERNATIVE RATE FILING PROCEDURE FOR SMALL UTILITIES	))))	CASE NO. 95-236

STAFF REPORT

Prepared By: Carl Salyer Combs
Public Utility Financial
Analyst, Senior
Water and Sewer Revenue
Requirements Branch
Financial Analysis Division

Prepared By: Sam Reid
Public Utility Rate
Analyst
Communications, Water and
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STAFF REPORT

ON

THELMA WASTE CONTROL, INC.

CASE NO. 95-236

A. Preface

On June 15, 1995, Thelma Waste Control, Inc. ("Thelma") filed an application with the Commission seeking to increase its water rates pursuant to the Alternative Rate Filing Procedure for Small Utilities. The proposed rates would generate approximately $7,715 annually in additional revenues, an increase of 35.5 percent over normalized test-year revenues of $21,709.

In order to evaluate the requested increase, the Commission Staff ("Staff") chose to perform a limited financial review of Thelma's operations for the test period, calendar year 1994. Since Thelma requested and received Staff assistance in preparing this application, the field review was done prior to the filing of the application. Carl Salyer Combs of the Commission's Division of Financial Analysis completed the review in Paintsville, Kentucky, on May 19, 1995. Mr. Combs is responsible for this Staff Report except for the sections on operating revenues and rate design which were prepared by Sam Reid of the Commission's Division of Rates and Research.

During the course of the review, Thelma was advised that all proposed adjustments to test-year expenses must be supported by some form of documentation, such as an invoice, or that all such adjustments must be known and measurable. Based upon the findings of this report, Staff recommends that Thelma be authorized to increase its annual operating revenue by $5,001.

Scope

The scope of the review was limited to obtaining information to determine whether reported test-period operating revenues and expenses were representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

B. Analysis of Operating Revenues and Expenses

Operating Revenues

Thelma's annual report indicated it received $20,892 from rates charged to 60 customers during the test year. In its application, Thelma reported 49 customers, 40 in the Fraley Subdivision and 9 in the Hughes Subdivision. Applying the current rates of $31.30 and $61.90, respectively, to the customers reported in the application, produces annual revenue of $21,709. Normalized test period revenue from rates is determined to be $21,709.

Operating Expenses

Thelma incurred, and the Staff-assisted application included, test-period operating expenses of $21,043. Thelma proposed to reduce that amount by $3,661. Staff's recommendations on those proposed adjustments to test-period operations are discussed below:

Electric Power

Thelma proposed to reduce its actual test-year electric expense of $2,934 by $934, but provided no explanation for the reduction. Therefore, Staff recommends that the actual annual test-year electric expense of $2,934 be included for rate-making purposes.

Chemicals

Thelma proposed to reduce reported test-year chemicals expense of $4,771 by $2,384, asserting that the operator has not been using chlorine tablets properly. Larry Updike, a sewer utility inspector with the Commission's Division of Engineering, is of the opinion that Thelma's annual projection of $2,387 is reasonable. Therefore, Staff recommends inclusion of annual chemicals expense of $2,387 for rate-making purposes.

Miscellaneous Supplies and Expenses

Thelma proposed to reduce actual test-year miscellaneous supplies and expense of $899 by $199, but provided no explanation for the reduction. Thelma documented test-year payments of $899 and its proposed reduction appears to be arbitrary. Therefore, Staff recommends that this adjustment be denied. Also, during the test year, Thelma paid a $600 invoice from Beckman Environmental Services Company of Cincinnati that was for services rendered in 1991. Staff recommends that this expense be excluded for rate-making purposes since the payment was for a prior-period expense. Therefore, annual miscellaneous supplies and expense of $299 has been included for rate-making purposes.

Outside Services

Thelma proposed to reduce actual test-year outside services expense of $1,289 by $644, but provided no explanation for the proposed reduction. After reviewing Thelma's test-period invoices, Staff was unable to see where a reduction to the actual expense incurred by Thelma would occur, and coupled with the fact that no explanation was provided for the proposed reduction, Staff recommends inclusion of annual outside services expense of $1,289 for rate-making purposes.

Amortization Expense

In its annual report, Thelma included no expense related to a construction permit, but proposed an annual expense of $500. Staff has learned that the permit was for construction of the treatment plants and represents an expense of an extraordinary and non-recurring nature. The cost of the construction permit should have been included in the total cost of the plants and depreciated over an appropriate period. In this instance, Staff recommends that the permit expense be amortized over 20 years which matches the amortization period of the debt associated with the plants and the period over which similar treatment plants are normally depreciated. Accordingly, annual amortization expense of $25[1] has been included for rate-making purposes.

Interest on Long-Term Debt

Thelma proposed to increase reported test-year interest on long-term debt expense of $5,460 by $446. After review of the

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1 $500/20 years = $25 annually

amortization schedule from the Kentucky Association of Counties Leasing Trust Program, Staff determined that a three-year average (1995-1997) of interest, plus other fees (administrative, credit, and fiduciary) amounts to $6,160[2]. Therefore, Staff recommends that annual interest on long-term debt expense of $6,160 be included for rate-making purposes.

Operations Summary

Based on the recommendations of Staff contained in this report, Thelma's operating statement would appear as follows:

Application	Test Period Application	Recommended Adjustments	Test Year Adjusted
OPERATING REVENUES	$ 20,892	$ 817	$ 21,709
OPERATING EXPENSES:			
Water Service	$ 180	$ -0-	$ 180
Electric Power	2,934	-0-	2,934
Chemicals	4,771	< 2,384>	2,387
Misc. Supplies & Exp.	899	< 600>	299
Treatment & Disposal	484	-0-	484
Routine Maint. Fee	2,600	-0-	2,600
Customer Records	160	-0-	160
Off. Supplies & Other	445	-0-	445
Outside Services	1,289	-0-	1,289
Insurance	888	-0-	888
Depreciation	6,189	-0-	6,189
Amortization Exp.	-0-	25	25
Taxes Other Than Inc.	204	-0-	204
Total Operating Exp.	$ 21,043	$< 2,959>	$ 18,084
OPERATING INCOME	$< 151>	$ 3,776	$ 3,625
OTHER DEDUCTIONS:			
Interest on L-T Debt	5,460	700	6,160
NET INCOME	$< 5,611>	$ 3,076	$< 2,535>

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[2]	
1995 Interest Expense	$ 6,384
1996 Interest Expense	6,160
1997 Interest Expense	5,937
Total	$18,481

$18,481/3 = $6,160 (3-year average)

C. Revenue Requirements Determination

The approach frequently used by the Commission to determine revenue requirements for small, privately-owned utilities is the calculation of an operating ratio.[3]

The ratio generally used by the Commission in order to provide for equity growth is 88 percent. In this instance, the use of an 88 percent operating ratio applied to the adjusted operating expenses, plus allowing a dollar-for-dollar coverage of reported test-year interest expense, results in a total revenue requirement of $26,710.[4] Therefore, Staff recommends an increase in annual revenues of $5,001 calculated as follows:

Revenue Requirement	$26,710
Less: Normalized Test-Year Revenues	21,709
Increase Required	$ 5,001

D. Rate Design

Thelma operates and maintains two sewage treatment plants. Thelma provides service to Fraley Subdivision at a rate of $31.30 per month and serves the Hughes Subdivision at a monthly rate of $61.90. In its application, Thelma proposed a rate of $46 for the customers served by the Fraley Subdivision and a monthly rate of $68 for the customers of the Hughes Subdivision. Thelma did not offer any justification as to why it proposed to increase the rates

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3 Operating Ratio = Operating Expense/Operating Revenue

4

Adjusted Operating Expense/Operating Ratio	$18,084/.88
Required Operating Revenue	20,550
Add: Reported Test-Year Interest Expense	6,160
Total Revenue Requirement	$26,710

to one subdivision by 47 percent and the other subdivision by 10 percent.

After a review of Thelma's operating expenses and rate design, Staff developed two possible rate designs. Thelma could continue to charge separate rates to the customers of each treatment plant. Based on the percentage of expenses allocated to each treatment plant in Thelma's proposed operating budget, Staff determined that the customers in the Fraley Subdivision should be responsible for paying 77.5 percent of the total revenue requirement while customers in the Hughes Subdivision would be responsible for 22.5 percent of the total revenue requirement. Separate rates will reduce cross subsidization between the two treatment plants. When applied to the annual revenue requirement of $26,710, the percentages result in a monthly rate of $43.13 for the customers in the Fraley Subdivision and a monthly rate of $55.65 for the customers in the Hughes Subdivision as shown in Attachment A.

Thelma's annual report does not set out separate expenses for the two treatment plants. The revenue requirement determined to be reasonable in this case is determined from the overall operation of the utility. Therefore, Staff developed a flat monthly rate that would be charged to all customers served by Thelma. The result is a monthly rate of $45.43 for all customers as set out in Attachment A.

After a complete review of all information available, Staff recommends that all customers served by Thelma pay a monthly rate of $45.43 as set out in Appendix A which will produce the revenue requirement recommended in this report.

E. Signatures

Carl Salyer Combs

Prepared By: Carl Salyer Combs
Public Utility Financial
Analyst, Senior
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Requirements Branch
Financial Analysis Division

Sam Reid Jr.

Prepared By: Sam Reid
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Communications, Water and
Sewer Rate Design Branch
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ATTACHMENT A

THELMA WASTE CONTROL, INC.
Case No. 95-236

Percentage of Revenue Based on the Application Proposed Operating Budget

	Fraley Subdivision	Hughes Subdivision	Total
Expenses	21,557	6,130	27,687
Less Principle	(3,520)	(880)	(4,400)
	18,037	5,250	23,287
	77.5%	22.5%	100%

Revenue Requirement $26,710		
	$20,700	$6,010
Divide by Customers	÷ 40	÷ 9
Annual Revenue	$517.51	$667.75
Divide by 12 Months	÷ 12	÷ 12
Monthly Bill	$ 43.13	$ 55.65

THELMA WASTE CONTROL, INC.

Flat Rate Design

Revenue Requirement	$26,710
Divide by Customers	÷ 49
Annual Revenue per Customer	$545.10
Divide by 12 Months	÷ 12
Monthly Bill	$ 45.43

APPENDIX A

TO STAFF REPORT CASE NO. 95-236

The following rates and charges are recommended for the customers of Thelma Waste Control, Inc.

MONTHLY RATES:

All customers	$45.43 per month