

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF MOCKINGBIRD VALLEY)
SANITATION, INC. FOR APPROVAL OF THE) CASE NO.
TRANSFER OF THE MOCKINGBIRD VALLEY) 2001-187
SANITATION, INC. WASTEWATER TREATMENT)
PLANT TO THE OLDHAM COUNTY SANITATION)
DISTRICT)

ORDER

On June 18, 2001, Mockingbird Valley Sanitation, Inc. (“MVS”) and Oldham County Sanitation District (“OCSD”) (collectively “the Joint Applicants”) applied for Commission approval of OCSD’s purchase of MVS’s wastewater treatment and collection system.

On July 11, 2001, Commission Staff propounded interrogatories and requests for production of documents to the Joint Applicants. The Joint Applicants responded to those requests on July 18, 2001. The Commission granted the Attorney General’s (“AG”) motion for intervention on July 24, 2001. The AG has stated that he would not sponsor testimony at any hearing of this matter and that he did not have any data requests for the applicants.

Therefore, having considered the application and the evidence of record, the Commission finds that:

1. OCSD is a sanitation district created pursuant to KRS Chapter 220. Its offices are located at 7311 Highway 329, Suite 542, Crestwood, Kentucky.¹

¹ Application, para. 3.

2. OCSD has purchased a sewage treatment system in the past and currently operates that, and other, systems.²

3. There is currently pending litigation between OCSD and this Commission regarding the Commission's jurisdiction over OCSD. In a June 20, 2001 decision, the Franklin County Circuit Court ruled that OCSD is subject to this Commission's jurisdiction.³ However, OCSD has appealed that decision to the Kentucky Court of Appeals.

4. For the 12-month period ending June 30, 2001, OCSD reported revenues of \$2,071,906 and expenses of \$472,164, resulting in net income of \$1,599,742. Included in OCSD's reported operating revenue are payments from the Oldham County Fiscal Court in the total amount of \$741,953 and a Department of Local Government Draw of \$1,041,974.⁴

5. As of June 30, 2001, OCSD reported total assets of \$4,849,248 and long-term liabilities of \$1,915,000.⁵

6. John Bennett, a licensed engineer in the state of Kentucky, is OCSD's chief engineer. His resume states that he has extensive experience in wastewater

² The Application of Covered Bridge Utilities, Inc. for Approval of the Transfer of the Covered Bridge Wastewater Treatment Plant to the Oldham County Sanitation District, Case No 1999-496 (Ky. P.S.C. March 13, 2000). The Commission approved the transfer of Covered Bridge to OCSD in that case.

³ See Oldham Co. Sanitation Dist. v. Public Service Commission, Civil Action No. 00-CI-480 (Div. I, June 20, 2001).

⁴ Response to Interrogatory No. 3.

⁵ Id.

treatment.⁶ OCSD's technical and professional employees are unchanged since the Commission issued its decision in The Application of Covered Bridge Utilities, Inc. for Approval of the Transfer of the Covered Bridge Wastewater Treatment Plant to the Oldham County Sanitation District, Case No. 1999-496 (Ky. P.S.C. March 13, 2000).⁷

7. MVS is a private sewer company subject to this Commission's jurisdiction. It is a Kentucky corporation. Myra K. Schurek is the president of MVS.⁸ It began operating on July 7, 1978.⁹

8. MVS provides sewer services to 43 customers located in Mockingbird Valley subdivision, LaGrange, Oldham County, Kentucky.¹⁰

9. MVS has no employees.¹¹

10. As of December 31, 2000, MVS reported utility plant of \$123,873 and accumulated depreciation of \$108,947, which results in net utility plant of \$14,926.¹² In addition, the only liability MVS reported is a loan of \$184,489 owed to Ms. Schurek.¹³ In

⁶ Application, para. 5 and Exh. D.

⁷ July 23, 2001 letter from Edward L. Schoenbaechler to Thomas M. Dorman.

⁸ Application, para. 1.

⁹ Mockingbird Valley Sanitation 2000 Annual Report, p. 1.

¹⁰ Id., pp. 1 and 12.

¹¹ Id., p. 1.

¹² Id., p. 4.

¹³ Response to Interrogatory No. 8(a)(2).

Case No. 94-034, Commission Staff determined that MVS had not received prior Commission authorization to incur this indebtedness as required by KRS 278.300(1).¹⁴

11. For the calendar year ending December 31, 2000, MVS recorded operating revenues of \$22,845 and utility operating expenses of \$21,226 resulting in net operating income of \$1,619.¹⁵

12. The Joint Applicants executed the asset purchase agreement on June 14, 2001.¹⁶

13. An independent appraiser, hired by OCSD, performed an appraisal of MVS's system utilizing replacement cost method. Based upon this appraisal, OCSD determined that a reasonable estimate of the value of MVS's assets was \$64,304, which is the sales price reached by the parties through negotiations.¹⁷

14. OCSD is paying \$49,378 above the December 31, 2000 net book value for MVS's assets. However, OCSD does not believe that MVS's net book value is related to market value or replacement costs.¹⁸ OCSD intends to seek rate recovery of the total purchase price, which includes the resulting acquisition adjustment. According to

¹⁴ See The Application of Mockingbird Valley Sanitation, Inc. for a Rate Adjustment Pursuant to the Alternative rate Filing Procedure for Small Utilities, Case No. 94-034, Staff Report at 6 (released April 18, 1994).

¹⁵ MVS Annual Report, p. 8.

¹⁶ See Asset Purchase Agreement.

¹⁷ Response to Interrogatory No. 12(a); see Asset Purchase Agreement.

¹⁸ Response to Interrogatory No. 12(b).

OCSD, it believes that the service rate can be maintained at the current level or even reduced through regional consolidation.¹⁹

15. Under the terms of the asset purchase agreement, OCSD will purchase all of MVS's assets. The agreement, however, refers to some assets that will be excluded from the sale.²⁰ OCSD stated in response to Commission Staff's interrogatories that no tangible personal property was included in the sale.²¹

16. The agreement states further that OCSD would assume MVS's rights and interests to contracts, agreements and leases.²² However, OCSD stated that it would assume none of MVS's contracts in this sale.²³ Also, OCSD will assume none of MVS's debts or liabilities.²⁴

17. The agreement contains several special provisions. First, OCSD will provide free sewer service to Myra K. Schurek at 1115 Cedar Point Road. Second, OCSD will decommission the plant and return the land to a level grade should it discontinue its operation. Third, OCSD will relocate the water meter for the plant to another location at its expense.²⁵

¹⁹ Response to Interrogatory No. 12(c).

²⁰ Asset Purchase Agreement, pp. 1-2.

²¹ Response to Interrogatory No. 5.

²² Asset Purchase Agreement, p. 2.

²³ Response to Interrogatory No. 6.

²⁴ Response to Interrogatory No. 8(a)(1).

²⁵ Asset Purchase Agreement, para. 1.6.

18. OCSD believes that it may provide free service to Myra K. Schurek because that was one of the negotiated items in the sale for which OCSD will receive adequate consideration.²⁶

19. OCSD has the option of updating the existing system or diverting sewage to its Heather Hill plant. It has not yet decided which option it will select, but hopes to decide in the next 2 years. OCSD agreed to reclaim the property upon decommissioning the plant because of the potential health hazards related to a sewage treatment system.²⁷

20. OCSD intends to adopt and charge MVS's rates. OCSD will not seek additional "assessments" as part of this acquisition.²⁸

CONCLUSIONS OF LAW

21. KRS 278.020(4) provides:

No person shall acquire . . . ownership of, or control . . . any utility under the jurisdiction of the commission . . . without prior approval of the commission. The commission shall grant its approval if the person acquiring the utility has the financial, technical, and managerial abilities to provide reasonable service.

22. KRS 278.020(5) provides that:

"The commission shall approve any proposed acquisition when it finds that the same is to be made in accordance with law, for a proper purpose and is consistent with the public interest."

²⁶ Response to Interrogatory No. 10.

²⁷ Response to Interrogatory No. 11.

²⁸ Response to Interrogatory No. 14. The Commission interprets this to mean "rates."

23. The Commission has ruled previously that OCSD has the financial, managerial and technical ability to operate acquired sewer systems.²⁹ OCSD has the financial, managerial and technical abilities to provide reasonable service to MVS's customers.

24. This transfer is in accordance with law, for a proper purpose and is consistent with the public interest.

25. KRS 278.170(1) provides that "No utility shall, as to rates or service, give any unreasonable preference or advantage to any person. . . ." A utility may, however, provide free service to officers, agents or employees. KRS 278.170(2). The asset purchase agreement states that OCSD shall provide free service to Myra K. Schurek. However, Ms. Schurek will not be an officer, agent or employee of OCSD.³⁰ Therefore, OCSD cannot rely upon the exception to KRS 278.170(1) to provide free service to Ms. Schurek. It is not relevant that this was a negotiated item in the sale. The Commission is bound by KRS 278.170 to prevent unreasonable discrimination, such as in this case.

26. Pursuant to the Franklin County Circuit Court's order in Oldham Co. Sanitation Dist. v. Public Service Commission, Civil Action No. 00-CI-480 (Div. I June 20, 2001), OCSD is now subject to this Commission's jurisdiction, pending final litigation of that case.

27. When the sale of a utility results in a purchase price greater than the original cost less accumulated depreciation (net book value), the difference between the purchase price and the net book value is accounted for as a plant acquisition

²⁹ See Covered Bridge, Case No. 1999-496.

³⁰ Response to Interrogatory No. 10.

adjustment. The proposed journal entry filed by the OCSD to effect the transfer records plant at the purchase price. The correct journal entry to be made by OCSD is a debit to Utility Plant in Service for \$123,873.16, a credit to Accumulated Depreciation for \$108,947.19 plus the depreciation for 2001 through the date of the transfer, a credit to Cash for \$64,304, and a debit to Utility Plant Acquisition Adjustments to balance the journal entry. Since the acquisition adjustment relates to the utility plant investment, it should be amortized over the remaining life of the assets. The amortization may be recorded in account 406, Amortization of Utility Plant Acquisition Adjustments. However, the Commission finds that the amortization of the acquisition adjustment should be approved in this proceeding for accounting purposes only, with the decision on rate-making treatment deferred to the next rate proceeding.

28. In Case No. 9059,³¹ the Commission determined that “The burden of proof is upon the utility to justify its investment at the price in excess of the net original cost based on economic and quality of service criteria.” To meet this burden of proof, the Commission established the criteria a utility must meet in order to recover any investment in excess of the net original cost (“plant acquisition adjustment”). OCSD is given notice that in order for it to recover through rates its plant acquisition adjustment it must present evidence to show that the purchase price of MVS meets the following criteria:

- a. The purchase price was established upon arms length negotiation.

³¹ An Adjustment of Rates of Delta Natural Gas Company, Inc., Case No. 9059, (Ky. P.S.C. Sept. 11, 1985).

b. The initial investment, plus the cost of restoring the facilities to required standards, will not adversely impact the overall costs and rates of the existing and new customers.

c. Operational economies can be achieved through the acquisition.

d. The purchase price of utility and non-utility property can be clearly identified.

e. The purchase price will result in overall benefits in the financial and service aspects of the utility's operations.

IT IS THEREFORE ORDERED that:

1. The proposed acquisition is approved as of the date of this Order.

2. Within 30 days of the date of the transfer, OCSD shall file the journal entry made to record the transfer.

3. MVS shall be responsible for submitting to the Commission a financial and statistical report, as described in Administrative Regulation 807 KAR 5:006, Section 3, for the period in calendar year 2001 it owned and operated the transferred assets.

4. OCSD shall include MVS in its 2001 financial and statistical report, as described in Administrative Regulation 807 KAR 5:006, Section 3, for the period in calendar year 2001 it owns and operates the transferred assets. This report must be based upon the accounts set up in conformity with the Uniform System of Accounts. Commission Staff is available to meet with or assist OCSD regarding this accounting system.

5. MVS shall immediately notify this Commission of the date it ceases operations and the date the corporation is dissolved.

6. Within 10 days of the date of this Order, OCSD shall file an adoption notice in accordance with Administrative Regulation 807 KAR 5:011.

7. Within 30 days of the date of this Order, OCSD shall file an amended tariff for the MVS system.

8. OCSD shall not provide free sewage service to Myra K. Schurek because to do so is a violation of KRS 278.170(1).

Done at Frankfort, Kentucky, this 15th day of August, 2001.

By the Commission

ATTEST:


Executive Director