

STAFF REPORT  
ON  
SHADOW WOOD SUBDIVISION SEWER SERVICE  
CASE NO. 2001-423

**FILED**  
APR 01 2002  
PUBLIC SERVICE  
COMMISSION

Pursuant to 807 KAR 5:076 Section 3, Shadow Wood Subdivision Sewer Service ("Shadow Wood") by letter date November 22, 2000, requested Commission Staff ("Staff") assistance in the preparation of a rate application. Karen Harrod and Scott Lawless of Staff responded to this request by performing a field review at Shadow Wood's office. The purpose of the review was to inspect Shadow Wood's books and records and gather information to formulate a rate application. The period reviewed was the year ended December 31, 2000, the test year. The scope of the review was limited to obtaining information as to whether the test year operating revenues and expenses were representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

During the field visit Shadow Wood noted that mounting legal fees related to Case Number 2000-379 was the primary reason rate relief was needed. It was agreed by Staff and Shadow Wood that it would be most appropriate to postpone the filing and processing of the rate application until the Commission had ruled on Case Number 2000-379 as that ruling would have a direct impact on the rate proceeding.

The initial field visit was conducted on April 19, 2001. Evidence was compiled from that point forward until October 29, 2001, when a completed application was delivered to Shadow Wood for its review. That application calculated a monthly flat rate of \$19.91 to be charged to each customer per 12,000 gallon residential equivalent and a

monthly surcharge of \$786.40 to be charged for five years to The Harbor at Harrod's Creek Condominium Association ("Association"). The surcharge was to cover Shadow Wood's cost of Case Number 2000-379.

Shadow Wood revised the application and submitted it to the Commission for consideration on December 3, 2001. The revised application calculated the monthly flat rate per residential equivalent to be \$50.40. It also requested two surcharges to be assessed against the Association. The first would be a one-time charge of \$58,962.95 to cover the cost of Case Number 2000-379. The second is a monthly charge of \$2,083.33 to be collected for one year to cover budgeted legal fees for the year 2002.

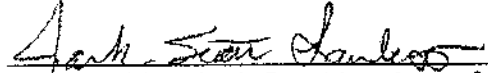
This report summarizes Shadow Wood's requests and Staff's recommendations. Staff's recommendations in this report result in rates different than those included in the assisted application due to additional information provided by Shadow Wood. Staff now recommends that Shadow Wood be allowed to charge a flat monthly residential equivalent rate of \$21.23 so as to produce annual revenue in the amount of \$75,374 and a monthly surcharge of \$3.39 to be applied to all customers for five years.

Attachment A of this Report details Shadow Wood's proposed pro forma operating income statement wherein test year revenues and expense were adjusted to reflect pro forma operations as projected by Shadow Wood. Attachment B details Staff's recommended adjustments to test year operations and provides explanation of all adjustments proposed by Shadow Wood and recommended by Staff. Attachment C compares the revenue requirement and rate calculations of Shadow Wood and Staff. Attachment D addresses the requested and recommended surcharge amounts.

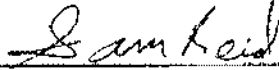
Sam Reid is responsible for all revenue adjustments and rate design issues.

Scott Lawless determined the revenue requirements.

Signatures



Prepared by: Jack Scott Lawless, CPA  
Financial Analyst, Water and Sewer  
Revenue Requirements Branch  
Division of Financial Analysis



Prepared by: Sam Reid  
Rate Analyst, Communications, Water,  
and Sewer Rate Design Branch  
Division of Financial Analysis

ATTACHMENT A  
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 SHADOW WOOD'S REQUESTED OPERATIONS

	Test Year	Adjustments	Pro forma
<b>Operating Revenues</b>			
Sewer Service Revenues	75,717		75,717
<b>Total Operating Revenue</b>	<u>75,717</u>	<u>-</u>	<u>75,717</u>
<b>Operating Expenses</b>			
<b>Operation and Maintenance</b>			
Administrative Salary	49,313	(19,313)	30,000
Bookkeeping		6,000	6,000
Rent		9,600	9,600
Telephone		1,320	1,320
Utilities		428	428
Other Expenses	1,411		1,411
Labor and Expense	8,948		8,948
Fuel and Power	14,962	(172)	14,790
Chemicals	251		251
Maintenance of Plant	35,449	(9,583)	23,000
		(2,000)	23,000
Insurance Expense	767	425	1,192
Miscellaneous	6,143	(5,292)	851
<b>Total Operation and Maintenance</b>	<u>117,244</u>	<u>(18,687)</u>	<u>98,657</u>
Depreciation	13,248	1,840	18,030
		2,942	18,030
Contribution to Connection Reserve		27,000	27,000
Contribution to Equipment Replacement		3,786	3,786
Taxes Other Than Income	3,315	(1,246)	2,069
<b>Total Operating Expenses</b>	<u>133,807</u>	<u>15,735</u>	<u>149,542</u>
<b>Net Operating Income</b>	<u>(58,090)</u>	<u>(15,735)</u>	<u>(73,825)</u>

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STAFF'S RECOMMENDED OPERATIONS

	Test Year	Adjustments	Ref.	Pro forma
<b>Operating Revenues</b>				
Sewer Service Revenues	75,717			75,717
<b>Total Operating Revenue</b>	<u>75,717</u>	<u>-</u>		<u>75,717</u>
<b>Operating Expenses</b>				
<b>Operation and Maintenance</b>				
Administrative Salary	49,313	(45,713)	A	3,600
Bookkeeping		1,200	B	1,200
Rent		1,863	C	1,863
Telephone		1,320	D	1,320
Utilities		428	E	428
Other Expenses	1,411			1,411
Labor and Expense	8,948			8,948
Fuel and Power	14,962	(172)	F	14,790
Chemicals	251			251
Maintenance of Plant	35,449	(9,383)	G	23,866
		(2,000)	G	
Insurance Expense	767	(375)	H	1,192
		800	H	
Miscellaneous	6,143	(5,202)	I	851
<b>Total Operation and Maintenance</b>	<u>117,244</u>	<u>(57,524)</u>		<u>59,720</u>
Depreciation	13,248	(13,248)	J	
		4,540	J	4,540
Contribution to Connection Reserve		-	K	-
Contribution to Equipment Replacement		-	L	-
Taxes Other Than Income	3,315	(1,246)	M	2,069
<b>Total Operating Expenses</b>	<u>133,807</u>	<u>(67,478)</u>		<u>66,329</u>
<b>Net Operating Income</b>	<u>(58,090)</u>	<u>67,478</u>		<u>9,388</u>

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A) Administrative Salary. During the test year Shadow Wood reported an owner/manager fee of \$49,313. This amount is shown as "Administrative Salary" in the application. The amount represents allocations of test year expenses incurred by Fourth Avenue and Long Corporation for salaries, employee benefits, insurance, depreciation, utilities, rent, and telephone expenses. The allocations were based on test year revenues of Fourth Avenue, Long Corp, and Shadow Wood. The amounts allocated to Shadow Wood are detailed as follows:

Salaries	\$35,346
Employee Benefits	3,157
Insurance	6,203
Depreciation	1,259
Utilities	970
Rent	1,833
Telephone	<u>545</u>
Total	<u>\$49,313</u>

At Attachment A of its application Shadow Wood proposed to adjust some of these items but included only the adjustment for Salaries on the line labeled "Administrative Salaries". The remaining adjustments are included on the lines labeled Bookkeeping, Rent, Telephone, and Utilities. Employee benefits, insurance, and depreciation as shown above were not included in pro forma operations.

Shadow Wood proposes to recover an administrative salary totaling \$30,000 annually. It claims the amount is necessary for compensation to the owner/manager for work related to Shadow Wood's on going litigation with the State's Division of Water and The Harbor at Harrod's Creek Condominium Association ("The Harbor"). To substantiate the requested amount, Shadow Wood provided salary survey information

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of full-time administrative positions. Shadow Wood argues that if the proposed salary is not included in rates the Commission should include the cost of attorneys and accountants performing these duties.

It is Staff's position that the owner/manager fee of \$3,600 is appropriate compensation for overseeing the daily operations of a small sewer utility. Staff understands that the duties of the owner/manager will vary from time to time but maintains that the position does not constitute full-time employment. Involvement of the owner/manager with ongoing litigation falls within the responsibilities of the owner/manager. In the past the Commission has limited the owner/manager fee to \$3,600. There is no need to deviate from that practice in this case.

In addition, Staff's recommended pro forma operations include provisions for maintenance, bookkeeping, accounting, billing, and collection service fees. That leaves only administrative duties to be performed by the owner/manager in return for the owner/manger fee.

B. Bookkeeping. Shadow Wood proposed annual bookkeeping fees of \$6,000. The basis for the adjustment was presented in the form of an invoice from its CPA, Buetow, LeMastus & Dick. The invoice totaled \$6,000 and was "for professional services rendered from March 17, 2001 through September 5, 2001". It stated that the services performed were "accounting assistance, preparation of property tax returns and PSC audit".

The invoice from Buetow, LeMastus & Dick may include costs that warrant recovery as a part of recurring accounting fees, rate case expense, or fees from Case

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2001-379. The utility's response to Items 4, 5, and 6 of Commission Order of February 25, 2002, fails to identify the costs associated with these services. Staff recommends therefore that the proposed adjustment be denied.

It is Staff's opinion that Shadow Wood be allowed to recover a reasonable amount for bookkeeping services. During the test year an employee of Fourth Avenue performed these services. A portion of the employee's salary was included in the test year allocation as discussed in Item A. Staff determined that the employee spent 10 hours per month performing bookkeeping services for Shadow Wood. Staff recommends that \$10 per hour be used to determine bookkeeping fees allowable in this case. That results in an annual expense of \$1,200. The hourly rate is \$1 per hour higher than allowed by the Commission for bookkeeping services of a similarly situated utility in Case Number 1999-331.

C) Rent. During the test year Fourth Avenue paid rent for office space in the amount of \$8,184. Of that amount it allocated \$1,833 to Shadow Wood.

In its application Shadow Wood proposed to increase that amount to \$9,600 stating that its operations were the sole reason for Fourth Avenue maintaining its office, and therefore, all rental charges should be reflected in Shadow Wood's expenses. Shadow Wood calculated the proposed amount on the determination that 600 square feet of office space is required and the average cost of rent per square foot is \$16 ( $\$16 \times 600 = \$9,600$ ). Since the application was filed Shadow Wood has found alternative office space at a cost of "\$1,200 per year plus expenses".



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Staff is of the opinion that Shadow Wood is entitled to recover a reasonable amount for rent expense, but that the requested amount of \$9,600 is excessive and unwarranted. Shadow Wood shares an office with Fourth Avenue and Long Corp. at 2036 Bashford Manor Lane, Louisville, Kentucky. Each should share in rental fees. During its field visit Staff determined that approximately a quarter of the leased space was used by Shadow Wood. Therefore, Staff recommends it be allocated a quarter of the rental fee. The monthly rental fee is \$620.85 resulting in an annual allocation of \$1,863 ( $\$620.85 \times 12 \text{ months} / 4$ ).

Shadow Wood's argument centers on the fact that Fourth Avenue maintains the office for the sole purpose of operating Shadow Wood. However, Fourth Avenue and Long Corp. continue to use the office space as their headquarters and there are operations other than Shadow Wood's being run from that location. Therefore, the rent should be shared. If Fourth Avenue decides to close its offices, Shadow Wood should find more cost efficient means of renting office space.

The \$1,200 plus expenses rental fee included in Shadow Wood's response to Commission Order, fails to meet the known and measurable test since neither the details of the agreement nor its "plus expenses" rider were presented. Absent this information Staff recommends that the Commission approve the allocation of \$1,863 for office rent.

D) Telephone. Test year telephone expense was allocated to Shadow Wood in the amount of \$545. Shadow Wood proposed to increase that amount to \$1,320. The test year allocation includes portions of office phone lines and long distance services. The

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proposed amount is based on the cost of one business line with call forwarding (\$70 per month) and one cellular service (\$40 per month).

Shadow Wood maintains that the proposed amount is reasonable as the owner/manager needs to be accessible at all times in case of emergency. With call forwarding a call can be forwarded to the cellular number for prompt attention in the event that the owner/manager is not in the office.

Owning and managing a small sewer operation is not a full time position but someone is required to be available at all times in case of emergency. Therefore, Staff agrees and recommends that the requested amount be approved.

E) Utilities. Test year office utilities were allocated to Shadow Wood in the amount of \$970. Shadow Wood proposed to reduce this amount to \$428. The proposed amount was determined by allocating a quarter of the total test year payments made to LG&E and Louisville Water Co. in the amounts of \$1,589 and \$122, respectively, for utility services at 2036 Bashford Manor Lane, the headquarters of Fourth Avenue, Long Corp., and Shadow Wood.

Staff agrees with the adjustment and recommends that it be approved as it directly coincides with Staff's recommendation of pro forma rental fees.

F) Fuel and Power. Test year fuel and power was reported at \$14,962. Review of information provided by LG&E indicates that test year payments had been received in the amounts of \$994 and \$13,796 in return for services at 5702 Captain's Quarters Rd. Lift Station and 5497 Forest Lake Dr. Sewer Treatment Plant, respectively. Shadow

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Wood proposed to decrease test year expenses to reflect those payments. Staff agrees and recommends that the proposed adjustment be accepted.

G) Maintenance of Plant. Test year maintenance of plant totaled \$35,449. Shadow Wood proposed to reduce the amount by \$9,583 for expenditures related to depreciable assets that were erroneously recorded as expenses and \$2,000 to reflect the five year amortization of non-recurring tree removal expense.

The assets purchased were a yard hydrant for \$764, flow meter for \$3,500, and air drops, diffusers, and blower in the total amount of \$5,319. Staff agrees that these amounts should be eliminated from maintenance of plant and recovered through a provision for depreciation.

Included in the test year amount was \$2,500 for tree removal. This amount is non-recurring and should therefore be amortized to "smooth" its effects on rates. Staff agrees with the proposed five-year amortization period and recommends that the Commission accept the adjustment decreasing test year expenses by \$2,000 ( $\$2,500 \text{ total cost} / 5 \text{ years} = 2,500 \text{ total cost}$ ).

H) Insurance Expense. During the test year insurance expense was reported at \$767. The amount included premiums for 1999 and 2000 flood insurance coverage. Shadow Wood proposed to decrease test year expenses by \$375, the amount of the 1999 premium, so that only one year of expense was included in pro forma operations. Staff agrees with the adjustment and recommends that it be approved by the Commission.

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Shadow Wood further proposed to increase test year expenses for premiums paid to Langan Co. for property and general liability insurance coverage in effect for the year ended December 1, 2001. Shadow Wood's portion of the premiums paid to Langan total \$800.

At Item 10 of its response to Commission Order dated February 25, 2002, Shadow Wood states that insurance premiums have increased drastically since the filing of its application. In support of its position Shadow Wood provided copies of insurance billing statements. However, the information provided is inadequate as to the nature and amounts of the stated premiums. Therefore, Staff recommends that the Commission approve Shadow Wood's original adjustment of \$800.

I) Miscellaneous Expense. During the test year miscellaneous expense was reported at \$6,143. Of that amount \$4,292 and \$1,000 represents payments to 621 Law Partners and Hugh Moore, respectively, for professional services render in Case 2000-379. Shadow Wood eliminated these amounts from test year operating expenses and proposed to include them as a part of the proposed surcharge. Staff agrees that the amounts should be eliminated from miscellaneous expense. The items are included in the discussion at Attachment D of this report as they relate to the proposed surcharge.

J) Depreciation Expense. Test year depreciation expense was reported at \$13,248. Of that amount \$4,814 is related to the plant replacement of 1980. For depreciation purposes that plant had a useful life of 20 years. The test year was the final year of

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depreciation taken on this asset. Therefore, this amount should be eliminated when determining pro forma depreciation expense.

The remaining \$8,434 is depreciation taken on the 1992 plant improvements. These improvements were necessary to extend service to The Harbortown Condominium Association, The Captain's Quarters restaurant, The Captain's Quarters Marina, and River Creek Subdivision.

Fourth Avenue developed the Captain's Quarters Marina and the River Creek Subdivision wherein it sold 32 lots. Parties other than Fourth Avenue developed the Captain's Quarters Restaurant and The Harbortown Condominiums.

Traditionally, this Commission has determined that when a developer invests capital for sewage facilities required to serve undeveloped properties, the investment is recouped through the sale of the developed property making it unnecessary and inappropriate to recover the cost through utility rates. Staff is of the opinion that the application of this methodology is appropriate in Shadow Wood's instance and has removed depreciation on these improvements when determining pro forma operations. In support of its recommendation Staff offers the following discussion.

Fourth Avenue was a direct beneficiary of the sewer plant improvements as they enabled Fourth Avenue to develop River Creek Subdivision and Captain's Quarters Marina. The plant improvement costs allocable to those developments should have been absorbed by those developments as though Fourth Avenue and Shadow Wood were independent entities. This point is illustrated by transactions between Fourth Avenue and the developer of The Harbortown Condominiums ("Harbortown").

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As Fourth Avenue did not have a direct interest in the development of Harbortown, Harbortown was charged \$48,000 (\$2,000 per unit) to tie into Shadow Wood's treatment plant facilities. This payment represents a contribution in aid of construction and should be used to offset the cost of the depreciable assets when setting rates.

After considering the transactions with Harbortown Staff is of the opinion that the transactions between Fourth Avenue and Shadow Wood were not performed at "arms length".

Shadow Wood argues that the improvements were financed through capital contributions of the two partners (Fourth Avenue and Long Corp.) with the intention that the investment would be recouped through sewer rates. It further argues that Fourth Avenue technically owns the 1992 assets and that in lieu of depreciation being included in utility rates, Fourth Avenue will charge a user fee to Shadow Wood for operating this portion of the collection system.

Shadow Wood's arguments are flawed. The financing of these plant improvements is no different than other developer investment to construct sewer facilities and should be treated no differently by the Commission.

The argument that Fourth Avenue owns the plant improvements and entitled to a user's fee to be paid by Shadow Wood has no merit. Pursuant to KRS 278.010 this Commission would regulate all collection services performed by Fourth Avenue. Fourth Avenue has never filed a proposed tariff with this Commission for such services. If such

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a tariff were filed, the Commission should exclude depreciation of the plant improvements on the same basis as previously stated with regard to Shadow Wood.

Depreciation has been adjusted to include depreciation on capital costs eliminated from test year expenses as discussed at Item G. Depreciation has also been adjusted to reflect the recovery of prior year capital expenditures that were erroneously included in expenses. The adjustment is detailed as follows:

Item	Amount	Life	Recovery
<b>Test Year</b>			
Yard Hydrant	\$764.26	10	\$76.43
Flow Meter	3,500.00	5	700.00
Air Drops, Diffusers, Blower	5,318.00	5	1003.72
<b>Previous To Test Year</b>			
Pump, 1998	2,110.00	5	422.00
Guide Rails, 1998	2,031.50	5	520.20
Alarm, 1998	850.00	5	170.00
Blower Motors, 1999	1,825.00	5	365.00
Blower and Exhaust Motor, 1999	1,045.23	5	209.05
Pump, 1999	1,900.00	5	392.00
Fencing, 1999	3,030.00	10	303.00
Pump, 1999	216.52	5	43.30
Chlorinator, 1999	1,347.50	5	<u>269.50</u>
<b>Total</b>			<b><u>\$4,540.20</u></b>

K) Contribution to Connection Reserve. Shadow Wood is required by its Kentucky Pollutant Discharge Elimination System Permit to connect to a regional collection facility when one is located within one mile of its sewage treatment facility. In its application Shadow Wood proposed to include a provision in rates of \$27,000 annually so as to accrue \$135,000 over five years to offset the construction cost of making such connection. In response to Commission Order of February 25, 2002, Item 16 E,

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Shadow Wood requested that this amount be amended to an annual recovery of \$46,600 or \$233,000 over five years.

The timing and costs of Shadow Wood's connection to a collection facility is uncertain. At present, there is no facility located within one mile of Shadow Wood's treatment facility nor is there a facility planned. Shadow Wood has not filed a certificate of convenience and necessity to construct a connection system with this Commission as required by KRS 278.020. Shadow Wood has not begun the design of a connection system nor has it received any cost estimates or bids of such system. It would be premature to allow Shadow Wood to collect construction costs through rates at this time as they are not known and measurable. Staff recommends that the proposed recovery be disallowed.

L) Contribution to Equipment Replacement. Shadow Wood proposed to increase test year expenses by \$3,875.85 for an equipment replacement provision. The amount was set at five percent of test year revenues.

Shadow Wood's adjustment is arbitrary and does not meet the known and measurable criteria for adjusting test year expenses. Staff recommends that it be denied.

M) Taxes Other Than Income. Test year taxes other than income were reported at \$3,315. Many of the amounts included in this account were payments of prior period taxes. In the application at Item K of Attachment A, Shadow Wood provided a listing of annual recurring taxes and permits totaling \$2,029. Shadow Wood proposed to adjust



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the test year amount to that level. Staff agrees with the adjustment and recommends it be accepted.

ATTACHMENT C  
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COMPARISON OF SHADOW WOOD'S AND STAFF'S REVENUE  
REQUIREMENT AND RATE CALCULATIONS

	Shadow Wood Requested	Staff Recommended	Difference Staff More/(Less)
Pro forma Operating Expenses	149,542	66,329	(83,213)
Divide by: 88 Percent Operating Ratio	88%	00%	0%
Revenue Required	169,934	75,374	(94,560)
Divide by: Residential Equivalents	281	296	15
12 Months	12	12	-
Flat Monthly Rate Per Residential Equivalent	50.40	21.23	(29.17)

Shadow Wood requested that its revenue requirements be determined by using an 88 percent operating ratio. This approach is frequently used by the Commission to determine revenue requirements for small, privately owned utilities. Staff agrees with its application and recommends that it be accepted.

The current rate design used by Shadow Wood is a flat rate monthly charge. Customers are classified into different categories and a rate is charged for customers in the same classification. The Classifications are single family residential, condos and commercial. The flat rate for a single family residential is \$26.50. The Harbor at Harrods Creek Condos are charged based on the number of bedrooms, \$19.90 for a two bedroom condo and \$26.50 for a three bedroom condo. The Commercial customers are charged based on a residential equivalent calculated from the customers water usage.

Staff recommends that the current rate design be revised. Staff recommends that residential customers be charged a flat monthly rate. Flat rates do not change from month to month within the user classification. Although a flat rate is used, the rate is based on the allocated sewage volume generated for that user classification. The rate

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COMPARISON OF SHADOW WOOD'S AND STAFF'S REVENUE  
REQUIREMENT AND RATE CALCULATIONS

for a single-family home is based on the average single-family home water use of approximately 400 gallons per day or 12,000 gallons per month.

Staff recommends that commercial customers will be billed on a residential equivalent basis. A commercial customers monthly average water usage is used to determine the residential equivalent unit (REU). A customer will be allocated one residential equivalent unit for each 12,000 gallons of water use. Example: the customer water usage averages 24,000 gallons per month. The customer will be allocated two REU ( $24,000 / 12,000 = 2$ ). For the calculation of the flat rate each single-family home will be allocated one REU.

The revenue requirement for Shadow Wood \$75,374 divided by the total number of REUs for all customers 296, results in a flat rate of \$21.23 per Residential equivalent unit.

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 REQUIREMENT AND RATE CALCULATIONS

Residential Customers	Number of Customers	Residential Equivalent unit	Monthly Flat Rate	Monthly Bill	Annual Revenue
The Harbor at Harrods Creek: 168 Condos	168	168	\$ 21.23		\$ 42,800
Harbor Town: 24 Condos	24	24	21.23		6,114
River Creek Subdivision:					
Houses	26	26	21.23		6,624
Shadow Wood Subdivision:					
Houses	40	40	21.23		10,190
<b>Commercial Customers</b>					
Harbor at Harrods Creek Clubhouse	1	2	\$ 21.23	\$ 42.46	\$ 510
Harbor Town Clubhouse	1	15	21.23	318.45	3,821
Captain's Quarters	1	20	21.23	424.6	5,095
Marina	1	1	21.23	21.23	255
<b>Totals</b>	<b>262</b>	<b>296</b>			<b>\$ 75,409</b>

ATTACHMENT D  
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REQUESTED SURCHARGES

In its application Shadow Wood proposed two surcharges to be assessed against the Association. The first surcharge is a one time charge of \$349.89 per member to raise \$58,962.95 (\$349.89 x 169 member) while the second is a monthly charge of \$12.33 with a duration of one year to raise \$25,000 (\$12.33 x 169 member x 12 months).

Requested One Time Surcharge of \$349.89.

Shadow Wood argues that the \$349.89 surcharge is necessary and just to cover expenses related to Commission Case No. 2000-379. The Association brought that case before the Commission alleging that Shadow Wood owed it \$141,726 in prior years over billings for sewer service. Shadow Wood now claims to have incurred costs totaling \$58,962.95 in its defense of those allegations. Shadow Wood argues that the Association should pay such costs as the Commission decided the Association had not met its burden of proof in the case. The costs include legal, miscellaneous, expert witness, and drafting fees in the amounts of \$47,557.06, 275.64, \$5,200.00, and \$5,930.25, respectively.

Staff agrees that expenses related to Case 2000-379 should be recovered by Shadow Wood as the Commission did not find in favor of the Association. Commission Staff initially felt that the entire amount should be allocated to the Association. However, since the preparation of the Staff assisted application, it has come to Staff's attention that a prior Commission Order may preclude such assignment of attorney's fees. Therefore, Staff allocated the amount to Shadow Wood's entire customer base.

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REQUESTED SURCHARGES

Staff agrees that the surcharge method is more appropriate than rolling the cost into general rates as the surcharge would cease without further Commission proceedings once all allowable costs were collected. However, it is also Staff's opinion that the proposed one-time surcharge is too burdensome. A more appropriate method would be to spread the recovery over a five-year period. This would serve to smooth the effects of its recovery and reduce rate shock.

If the Commission approves the five year surcharge, Staff is of the opinion that an interest component must be included in the calculation to offset the carrying costs of the unamortized balance carried on the books of Shadow Wood. In the absence of an alternative interest rate Staff recommends the Commission use the same four percent annual rate as used by the Commission in determining refund amounts in Case 2000-379.

To calculate the surcharge Staff reviewed the costs included in the requested amount of \$58,962.95 and made the following adjustments.

Staff reviewed legal invoices totaling \$45,494.31 from September 2000, through October 2001. Staff determined that \$43,089.31 of the total was directly related to Case 2000-379 and should be included in the surcharge.

Miscellaneous costs totaled \$275.64 and include fees for copying, mileage, and parking for library research. Staff recommends that this amount be included in the surcharge calculation.

Shadow Wood's requested amount included expert witness fees totaling \$5,200. The fees include \$3,000, \$1,500, and \$700 charged by Hugh Moore of Remax

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REQUESTED SURCHARGES

Properties, Putney Architecture, and Lexus Utilities, respectively. These amounts represent flat fees for services provided. Before any cost can be allowed in rates they must be shown to be reasonable. To make that determination detailed information must be provided with regard to specific work performed and time necessary for its completion. In addition, other independent vendor bids for similar services can be used for comparison purposes. The Commission requested such information with regard to the expert witness fees in its February 25, 2002, Order at Items 20, 21, and 22 but it was not provided. Shadow Wood has not met its burden of proof with regard to these expert witness fees. The Commission should deny them.

The drafting fees of \$5,930.25 were charged by Clay Long. The drafting fees were in return for the creation of a floor plan for each style of condominium unit located at The Harbor. The floor plans were entered into the record in Case 2000-379. Clay Long provided detailed time records and a vendor bid for the drafting services. After reviewing the detailed records Staff determined that only \$4,737.50 was for drafting services. The remaining charges were related to the general operation of Shadow Wood and should be covered by the owner/manager fee as previously discussed. Staff recommends that the Commission include \$4,737.50 in the surcharge calculation.

The surcharge is calculated as follows:

ATTACHMENT D  
STAFF REPORT CASE NO. 2001-423  
REQUESTED SURCHARGES

Legal	\$ 43,089
Miscellaneous	276
Drafting	<u>4,738</u>
 Total	 48,103
Annual Interest Rate	4%
Number of Payments	<u>60</u>
 Total Monthly Payment	 885.89
Divide by: Total Number of Customers	<u>202</u>
 Monthly Charge Per Customer	 <u>\$ 3.39</u>

Requested Monthly Surcharge of \$12.33.

Shadow Wood argues a \$12.33 monthly surcharge is necessary to cover ongoing litigation with The Harbor including The Harbor's intervention in this rate proceeding. The surcharge amount is based on legal costs totaling \$25,000.

Shadow Wood's proposal does not meet the known and measurable requirement for adjusting rates. Shadow Wood has not provided any information supporting the requested amount. The Commission should deny the request.

Shadow Wood should be allowed to recover costs of this rate case through amortization expense. However, Shadow Wood has not provided the appropriate cost information. That and other information concerning the \$25,000 legal fees was last sought at Item 27 of the Commission's Order dated February 25, 2002.