

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF B & H GAS)	CASE NO.
COMPANY, INC. FOR AN ALTERNATIVE RATE)	2020-00364
ADJUSTMENT)	

ORDER

On November 12, 2020, B & H Gas Company, Inc. (B & H) filed its application for an adjustment of its base gas rates pursuant to 807 KAR 5:076.¹ B & H is a Kentucky corporation regulated by the Commission as a utility under KRS 278.010(3)(b), and operates facilities that supply natural gas to approximately 261 customers residing in Floyd County.² B & H has not changed its base rates since 1992.³ B & H determined that its pro forma operations support a revenue requirement from base rates of \$184,482.⁴ The base rates B & H proposed produce annual base rate revenues of \$226,145, an increase of \$190,984, or 543.17 percent over normalized test-year base rate revenues of \$35,161.⁵

¹ B & H tendered its application on November 5, 2020. By letter dated November 9, 2020, B & H was notified that its application was rejected for filing due to certain filing deficiencies, which were subsequently cured. B & H's application was deemed filed as of November 12, 2020.

² Application, ARF Form 1 – Attachment SR – Reasons for Application.

³ Case No. 1991-00127, *The Application of B & H Gas Company, Inc. for Rate Adjustment Pursuant to the Alternative Rate Filing Procedure for Small Utilities* (Ky. PSC Jan. 13, 1992).

⁴ Application, ARF Form 1 – Attachment RR-OR – Revenue Requirement Calculation – Operating Ratio Method.

⁵ Application, ARF Form 1 – Attachment BA-DB – Billing Analysis - Declining Block Rates.

On November 30, 2020, the Commission, in response to a public comment that alleged that B & H's customer notice was illegible due to the small print, placed this case into abeyance until B & H mailed a legible notice to its customers and filed the same notice with the Commission. On December 2, 2020, B & H complied, allowing the case to proceed. To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated December 4, 2020, and found that pursuant to 807 KAR 5:076, Section 11, a Staff Report would not be issued and that the information needed to process this case would be obtained through the application and Commission Staff's Requests for Information.

There are no intervenors in this matter. B & H responded to two requests for information issued by Staff. On March 23, 2021, B & H filed a motion requesting that the hearing scheduled for March 30, 2021, be canceled and for leave to use Johnson County Gas Company's (Johnson County) base rates as part of the proposed transfer of B & H and Johnson County to Navitas KY NG, LLC.⁶ In its March 29, 2021 Order, the Commission granted B & H's motion to cancel the hearing and deferred the decision on the request to use Johnson County's rates until Case No. 2020-00396 was concluded. On April 27, 2021, the Commission issued a final order in Case No. 2020-00396, which found that B & H should use Johnson County's base rates because B & H can likely support rates that are higher than Johnson County's existing rates and Navitas KY requests to use the lower rates of Johnson County to reduce customer confusion and for ease of operations. This case now stands submitted to the Commission for a decision as

⁶ See Case No, 2020-00396, *Electronic Application of Navitas KY NG, Johnson County Gas Company, and B & H Gas Company for Approval of Acquisition, Transfer of Ownership, and Control of Natural Gas Utility Systems* (Ky. PSC Apr. 27, 2021).

to whether the rates of Johnson County produce rates in excess of the revenue requirement of B & H as a separate entity.

TEST PERIOD

The calendar year ended December 31, 2019, is being used as the test year to determine the reasonableness of B & H's existing and proposed base rates as required by 807 KAR 5:076, Section 9.

INCOME STATEMENT

B & H reported actual test-year operating revenues and expenses of \$139,889 and \$211,092, respectively.⁷ B & H proposed several adjustments to test-year revenues and expenses to reflect current and anticipated operating conditions, resulting in pro forma operating revenues of \$46,578 and pro forma operating expenses of \$179,327.⁸ The Commission's review of B & H's test-year operating revenues and expenses are set forth below.

Other Operating Revenues - B & H's application reported no Other Operating Revenues from fees and nonrecurring charges. In response to an interrogatory, B & H reported revenues from fees and nonrecurring charges of \$2,611.⁹ The Commission finds that test-year Operating Revenues should be decreased and Other Operating Revenues should be increased by \$2,611.

⁷ Application, ARF Form 1 – Attachment SAO-G –Schedule of Adjusted Operations – Gas Utility (Schedule of Adjusted Operations).

⁸ *Id.*

⁹ B & H's Response to Commission Staff's First Request for Information (Staff's First Request), Item 9.

Gas Cost Revenues - In order to remove revenues recovered through B & H's Gas Cost Recovery (GCR) mechanism, B & H proposed to reduce its test-year operating revenues from gas sales by \$93,311.¹⁰ The Commission's established ratemaking practice is to exclude gas costs that are recovered through the GCR mechanism from the calculation of utilities' base rates. The Commission finds B & H's removal of gas cost should be accepted.

Natural Gas Purchases and Transmission Fees - B & H proposed to reduce its test-year operating expenses by \$93,311 to eliminate its gas supply expense.¹¹ Given that natural gas purchases and transportation cost are recovered through the GCR mechanism, the Commission finds that B & H's proposed adjustment should be accepted.

Mapping Expenses - B & H proposed to increase its operating expenses by \$8,425 for mapping services.¹² According to B & H, its maps are updated as needed and were last updated in 1990.¹³ Expenses that are incurred intermittently should be normalized to prevent over-recovery. The Commission finds that a ten-year period is reasonable, and therefore B & H's proposed adjustment of \$8,425 should be reduced to \$843.

Meter Testing Expenses - B & H proposed to increase its operating expenses by \$4,000 to reflect estimated meter testing expenses.¹⁴ According to B & H, this adjustment is necessary because these expenses are "currently paid on behalf of B & H by [a] related

¹⁰ Schedule of Adjusted Operations.

¹¹ *Id.*

¹² Schedule of Adjusted Operations.

¹³ B & H's response to Commission Staff's Second Request for Information (filed Feb. 18, 2021) (Response to Staff's Second Request), Item 4.a.

¹⁴ Schedule of Adjusted Operations.

entity” and not recorded on B & H’s books.¹⁵ B & H provided its actual meter testing expenses for 2017-2019, which totaled \$2,616 for the testing of 10 meters in 2017.¹⁶

B & H’s actual expenses should be normalized over the three-year period. The Commission therefore finds that B & H’s proposed adjustment of \$4,000 should be reduced to \$872.

Bad Debt Expense - B & H proposed to increase its operating expenses by \$2,150 to include bad debt expense, estimated as 2 percent of residential gas sales.¹⁷ B & H stated that uncollectible accounts were not expensed during its test year and were included in accounts receivable.¹⁸ The Commission has determined that bad debt expense should be estimated based on the average bad debt percentage from 2017-2019, of 0.51 percent of gas sales.¹⁹ Accordingly, B & H’s proposed adjustment of \$2,150 should be reduced to \$986.

Rate Case Expenses - B & H proposed to increase its operating expenses by \$20,000 to include legal fees related to its rate case filings.²⁰ B & H included \$1,932 in legal fees related to the filing of Case No. 2018-00433,²¹ an ARF application that was dismissed because B & H never met the minimum filing requirements.²² These expenses

¹⁵ *Id.* and B & H’s Response to Staff’s First Request, Item 1.a.

¹⁶ B & H’s Response to Staff’s Second Request, Item 2.

¹⁷ Schedule of Adjusted Operations.

¹⁸ B & H’s Response to Staff’s Second Request, Item 4.c.

¹⁹ B & H’s Response to Staff’s Second Request, Item 4.d.

²⁰ Schedule of Adjusted Operations.

²¹ Case No. 2018-00433, *Application of B & H Gas Company for an Alternative Rate Adjustment* (Ky. PSC July 30, 2019).

²² B & H’s Response to Staff’s Second Request, Item 1.

are not properly recoverable in this filing. They were incurred outside the test year and do not represent costs likely to be incurred going forward. B & H stated that it had incurred \$475 of legal fees related to the current filing and estimated that it would incur an additional \$5,000, for a total recoverable rate case expense of \$5,475.²³ The Commission finds that B & H should only recover its actual rate case expense, which should be amortized over three years, and that its proposed adjustment of \$20,000 should be reduced to \$1,825.

Utilities Expense - B & H provided invoices for its allocated expenses, including utility bills for its affiliate-owned office space, which include charges for cable television.²⁴ These expenses are not recoverable from ratepayers. B & H's allocated portion of the cable charges are \$418. The Commission finds that B & H's test-year expenses should be reduced by \$418.

Summary Impact of Adjustments - After considering the test-year operating revenues and expenses, including appropriate adjustments found reasonable herein, the Commission has determined that the financial results of B & H's pro forma test-year operations would be as follows:

²³ *Id.*

²⁴ B & H's Response to Staff's First Request, Item 25 (redacted response to Item 25 was filed Jan. 21, 2021).

	Test-Year Operations	Pro Forma Adjustments	Pro Forma Operations
<u>Operating Revenue</u>			
Residential	107,590	(70,675)	36,915
Commercial & Industrial	32,299	(25,247)	7,052
Total Sales of Gas	139,889	(95,922)	43,967
Misc. Revenues		2,611	2,611
Total Operating Revenues	139,889	(93,311)	46,578
<u>Expenses</u>			
Gas Supply	93,311	(93,311)	-
Distribution	48,093	843	48,936
Customer Accounts		872	872
Customer Service and Informational Expenses		6,746	6,746
Administrative and General Expenses	51,247	41,059	92,306
Total O&M	192,651	(43,791)	148,860
Depreciation Expense	4,909		4,909
Taxes Other than Income	13,532		13,532
Income tax expense		5,439	5,439
Total Operating Expenses	211,092	(38,353)	172,739
Utility Operating Income	(71,203)	(54,958)	(126,161)

REVENUE REQUIREMENT DETERMINATION

The Commission has historically used an operating ratio approach to determine revenue requirements for small, privately owned utilities.²⁵ This approach is used

²⁵ An operating ratio measures the difference between operating revenues and operating expenses. It is defined by the following equation.

$$\text{Operating ratio} = \frac{\text{Operation \& Maintenance Exp. + Depreciation + Taxes}}{\text{Gross Revenues}}$$

The Commission has found that the operating ratio is a reasonable and necessary alternative to the rate of return method for calculating the allowable NOI for small investor owned utilities. Specifically, it has found that the rate of return method cannot be used because there is "no basis" upon which to determine a rate of return for these utilities, Case No. 95-236, *Application of Thelma Waste Control, Inc. for a Rate Adjustment Pursuant to the Alternative Rate Filing Procedure for Small Utilities* (Ky. PSC Apr. 15, 1996) at 6. Further, it has found that the operating ratio method is appropriate when plant investment is low and operating expenses are high, Case No. 7982, *Notice of Application of Fern Lake Company* (Ky. PSC Aug. 27, 1981) at 3.

because no basis for rate-of-return determination exists or the cost of the utility has fully or largely been recovered through the receipt of contributions. Given that B & H is a small gas distribution system, the Commission finds that this method should be used to determine B & H's revenue requirement.

As shown in the table below, B & H's pro forma operations, an allowance for income taxes, and an 88 percent operating ratio results in a revenue requirement from base rates of \$192,942, which is an increase of 338.83 percent or \$148,975 over revenues from existing base rates of \$43,967.

Pro forma Operating Expenses Before Income Taxes	\$ 167,301
Divide by: Operating Ratio	<u>88%</u>
Overall Revenue Requirement before Income Taxes	\$ 190,114
Less: Pro forma Operating Expenses Before Income Taxes	<u>\$ (167,301)</u>
Net Operating Income After Income Taxes	\$ 22,814
Add: Provision for State and Federal Income Taxes	\$ 5,439
Interest Expense	
Pro forma Operating Expenses Before Income Taxes	<u>\$ 167,301</u>
Total Revenue Requirement	\$ 195,553
Less: Other Operating Revenue	<u>\$ (2,611)</u>
Total Revenue Required from Rates for Service	\$ 192,942
Less: Revenue from Sales at Present Rates	<u>\$ 43,967</u>
Required Revenue Increase	<u>\$ 148,975</u>
Required Rev. Increase (% of Rev. at Present Rates)	<u>338.83%</u>

RATES AND RATE DESIGN

B & H proposed in its application to retain its rate design with a minimum charge for two Mcf in the first rate block, with two additional blocks for declining usage.²⁶ It later proposed, and the Commission approved upon the transfer of B & H to Navitas KY, to use the rates and rate structure of Johnson County to reduce customer confusion and for ease of operations. Based on the completion of the transfer and the revenue requirement found reasonable herein, the Commission finds the \$15 monthly customer charge and volumetric base rate of \$8.60 per Mcf is reasonable, do not produce excess revenues, and should be charged for service rendered on and after the date of the transfer closing.

TARIFF

B & H will not need to file revised tariff for this proceeding because its revised tariff was filed in compliance with Case No. 2020-00396.

SUMMARY

After consideration of the evidence of record and being sufficiently advised, the Commission finds that:

1. The rates proposed by B & H would produce revenues in excess of the amount found reasonable herein and should be denied.
2. The rates of Johnson County set forth in the Appendix to this Order do not produce revenues in excess of the amount found reasonable herein, are fair, just and reasonable and should be approved.
3. B & H's revised tariff has been filed in compliance with Case No. 2020-00396.

²⁶ Application, ARF Form 1 - Attachment CPR – Current and Proposed Rates.

IT IS THEREFORE ORDERED that:

1. The rates proposed by B & H are denied.
2. The rates and charges found reasonable herein and set forth in the Appendix to this Order are approved for service rendered by B & H on and after the date of this Order.
3. This case is closed and removed from the Commission's docket.

By the Commission



ATTEST:


Executive Director

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2020-00364 DATED SEP 10 2021

The following rates and charges are prescribed for the customers served by B & H.

All other rates and charges not specifically mentioned in this Order shall remain the same as those in effect under the authority of this Commission prior to the effective date of this Order.

RETAIL RATES:

	<u>Base Rate</u>	<u>Gas Cost Recovery Rate</u>	<u>Total</u>
Customer Charge	\$15.00		
All Mcf	\$8.60	\$ 7.2892 ¹	\$15.8892

¹ Gas cost approved effective August 1, 2021, in Case No. 2021-00278, *Electronic Purchased Gas Adjustment Filing of Navitas KY NG, LLC* (Ky. PSC Jul. 30, 2021).

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