

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the Matter of the Request of LW Sewer)
Corporation for a Rate Increase Pursuant to)
the Commission's Small Company Rate)
Increase Procedure)

Case No. SR-2005-0338
Tariff I.D. No. YS-2005-0897

**SUPPLEMENT TO RECOMMENDATION REGARDING
DISPOSITION OF SMALL COMPANY RATE INCREASE REQUEST**

COMES NOW the Staff of the Missouri Public Service Commission ("Staff"), by and through Counsel, and for its Supplement to Recommendation Regarding Disposition of Small Company Rate Increase Request states the following to the Missouri Public Service Commission ("Commission").

1. On May 19, 2005, this case was discussed at the Commission's Agenda session. During that discussion, Commissioners raised questions regarding three issues. The Staff's responses to the Commissioners' questions regarding those issues are set out in the document that is attached hereto and identified as Appendix A.

2. In addition to the responses included in Appendix A, the Staff will also have representatives at the Commission's May 26, 2005 Agenda session to answer any additional questions that the Commissioners may have.

WHEREFORE, the Staff respectfully submits this supplement to its recommendation and respectfully requests that the Commission issue an order in this case consistent with the recommendations set out on page 6 of the Staff's Official Case File Memorandum, which was filed in this case on May 13, 2005.

Respectfully Submitted,

DANA K. JOYCE
General Counsel

/s/ Keith R. Krueger

Keith R. Krueger
Deputy General Counsel
Missouri Bar No. 23857

Attorney for the Staff of the
Missouri Public Service Commission

P.O. Box 360
Jefferson City, MO 65102
573-751-4140 (telephone)
573-751-9285 (facsimile)
keith.krueger@psc.mo.gov (e-mail)

CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing have been mailed with first class postage, hand-delivered, transmitted by facsimile or transmitted via e-mail to all counsel and/or parties of record this 25th day of May 2005.

/s/ Keith R. Krueger

STAFF RESPONSES TO QUESTIONS RAISED BY THE COMMISSIONERS

LW SEWER CORPORATION - - - CASE NO. SR-2005-0338

May 25, 2005

ISSUE 1 – WATER SERVICE PROVIDER AND SERVICE DISCONNECT POLICIES

Commissioners asked who provides water service in LW Sewer's service territory; whether there is an agreement with the water service provider regarding discontinuance of service for non-payment of sewer service billings; and whether discontinuance of sewer service without a corresponding discontinuance of water service could create environmental problems. Commissioners also asked for a description of LW's policies regarding the discontinuance of sewer service.

Staff Responses: First, there is no central water service provider in LW's service territory. Rather, water service is provided through the use of private wells. As a result, there is no entity with which LW could enter into an agreement regarding discontinuance of water service for non-payment of sewer service billings.

The discontinuance of sewer service without a corresponding discontinuance of water service could certainly cause environmental problems – particularly for the involved structure. However, the Staff believes sewer utilities must still be able to have tariff provisions for the discontinuance of service for non-payment of their billings as a viable means of collecting their approved charges for service.

The Staff notes that LW notifies the local county department of health whenever sewer service is discontinued. The county health department then “condemns” the involved structure for occupancy purposes until sewer service is restored. As required by the Commission's rules, LW also provides the Water & Sewer Department with copies of any service disconnection notices. Copies of LW's "billing policy and non-payment procedure" and an example service disconnection notice are attached hereto as Attachments 1 & 2, respectively.

ISSUE 2 – SERVICE RELATED COMMENTS SUBMITTED BY MS. KELLNER

Commissioners asked whether Ms. Kellner's comments regarding a sewage overflow at a manhole near her residence had been addressed.

Staff Responses: On May 23, a representative of LW told Jim Russo of the Staff that LW had recently replaced the manhole and a section of main in the vicinity of Ms. Kellner's residence. Additionally, Staff members Steve Jungmeyer and Jerry Scheible conducted an inspection of LW's facilities on May 24 and confirmed that the manhole and main replacement had in fact been done. Mr. Jungmeyer and Mr. Scheible also talked with Ms. Kellner who said she was satisfied with LW's response to this situation and that no problems with the manhole have occurred since the replacements were done.

Regarding the issue of this matter not being addressed in the documents the Staff has submitted to either the tracking file or case file for LW's rate increase request, the Staff notes this was simply an oversight and that actions have been taken to ensure such an oversight does not occur in the future.

ISSUE 3 – CALCULATION OF SMALL COMPANY DEPRECIATION RATES

Commissioners asked whether the calculation of the depreciation rates being recommended for LW, which are the Staff's generic small sewer company depreciation rates applicable to LW's active plant accounts, include consideration of net salvage; and whether the subject depreciation rates were calculated in accordance with applicable Commission rules.

Staff Responses: No statute governs the manner in which depreciation rates for sewer (or water) companies are to be calculated. The only statute that specifically pertains to depreciation rates is Section 393.240, which authorizes the Commission to ascertain and determine the proper and adequate rates of depreciation. It does not address the treatment of the net salvage issue.

Likewise, no Commission rule governs the manner in which depreciation rates for sewer (or water) companies are to be calculated. The only rule that specifically pertains to depreciation is 4 CSR 240-10.020, Income on Depreciation Fund Investments. It does not address the treatment of the net salvage issue. More generally, Rule 4 CSR 240-61.020, Uniform Systems of Accounts – Sewer Companies, requires a Class C or D sewer company (such as LW) to use the *Uniform Systems of Accounts For Class C and D Sewer Utilities 1976*, issued by the National Association of Regulatory Utility Commissioners.

The Commission has, however, addressed the issue of the treatment of net salvage in the Reports and Orders that it issued in two recent rate cases. In its Third Report and Order in Case No. GR-99-315, issued January 11, 2005, the Commission discussed the net salvage issue at length, found that the accrual method of accounting for net salvage was just and reasonable, and ordered that the calculation of net salvage value for the determination of depreciation rates be done in accordance with Laclede Gas Company's recommendations. Two months later, the Commission followed the same reasoning in its Report and Order in the Empire District Electric Company rate case, Case No. ER-2004-0570, stating: "It is the policy of this Commission to return to traditional accounting methods for Net Salvage."

Historically, the Staff has maintained schedules of "generic" depreciation rates applicable to small water and sewer companies, which recognize a component for net salvage in the calculation of the rates. However, for most of those rates the "salvage component" has always been zero, for reasons discussed below. For example, the Staff's schedule of depreciation rates from 1998 for small water companies included rates for 35 plant accounts, but only three of those accounts included a salvage component that was not zero; and the schedule for small sewer companies included rates for 22 plant accounts, but only one of those accounts included a salvage component that was not zero. In all instances where a salvage component other than zero was included in the rate calculations the rate calculations assumed the existence of a positive net salvage value. When applied to the calculation of depreciation rates, positive net salvage actually lowers the depreciation rates and thus reduces depreciation expense. Conversely, negative net salvage has the impact of raising the depreciation rates and thus increases depreciation expense. An example of positive net salvage generally exists in transportation equipment accounts, which includes company vehicles. As noted above, the Staff is not aware of the generic small water and sewer company depreciation rates ever including a negative net salvage component.

There are three main reasons that this approach to calculating the depreciation rates for the small water and sewer companies has historically been used. First, most of the plant accounts have very small balances, if any, because much of the plant has historically been contributed to the utilities, and is therefore not included in rate base. Second, because of the small plant balances in most accounts, there has been very little experience in actual plant retirements being made in such accounts, which negatively affects the accuracy of establishing a salvage component for inclusion in the depreciation rate calculation. And third, the cost of removal has historically been assumed to equal the salvage value, which results in a salvage component of zero.

In the 2002-2003 time period, the Staff adjusted its schedules of depreciation rates applicable to small water and sewer companies to remove the salvage component from the calculation of the rates for all plant accounts, in order to be consistent with the policy in place at that time. However, because the small water and sewer company depreciation rates only included positive net salvage, as discussed above, this practice did not result in a reduction in depreciation expense to the small water and sewer companies.

Subsequent to the Commission's decision in the general rate case for The Empire District Electric Company, discussed above, the Staff has again adjusted its schedules of depreciation rates applicable to small water and sewer companies to include the positive net salvage components in the calculation of the rates for those plant accounts that had historically included such components in the rate calculation.

From an accounting perspective, net salvage has consistently been treated in accordance with the Uniform System of Accounts for small water and sewer companies, when retirements do occur. As a result, in some instances, the combination of the depreciation rates including a net salvage component of zero and the proper accounting treatment of retirements have resulted in special amortizations being included in a company's cost-of-service calculation. For example, a small sewer company's cost of closing a lagoon treatment facility was recently included in that company's cost-of-service as a special ten-year amortization. (In that situation the Department of Natural Resources had ordered the closing of the lagoon for environmental reasons.)

Regarding LW in particular, the plant accounts included on the recommended schedule of depreciation rates are ones that have historically had a net salvage component of zero, and the timing of adjustments that have been made to the Staff's schedules of depreciation rates for small water and sewer companies over the last several years has thus not affected those rates.

As noted above, the Staff's schedules of depreciation rates in small water and sewer company rate increase cases have recently been adjusted to comply with the Commission's most recent ruling on this matter in a general rate case. As also noted previously, the overall treatment of cost of removal/net salvage is consistent with the Uniform System of Accounts adopted by the Commission through its rules.