

**COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION**

IN THE MATTER OF:)	
)	
THE APPLICATION OF KENTUCKY-AMERICAN)	CASE NO. 2012-00520
WATER COMPANY FOR AN ADJUSTMENT OF)	
RATES ON AND AFTER JANUARY 27, 2013)	

APPLICATION, STATEMENT AND NOTICE

Kentucky-American Water Company states the following:

1. Kentucky-American Water Company (“Kentucky American Water”) is a corporation organized and existing under the laws of the Commonwealth of Kentucky with its principal office, place of business and post office address at 2300 Richmond Road, in Lexington, Fayette County, Kentucky.

2. Kentucky American Water is a wholly-owned subsidiary of American Water Works Company, Inc. (“American Water”) and is engaged in the distribution and sale of water in its Central Division, consisting of Bourbon, Clark, Fayette, Harrison, Jessamine, Scott and Woodford Counties and its Northern Division, consisting of Gallatin, Owen and Grant Counties. It currently owns, operates and maintains potable water production, treatment, storage, transmission and distribution systems for the purpose of furnishing potable water for residential, commercial, industrial and governmental users in its service territory.

3. To meet continuing demand for adequate service, Kentucky American Water has continued to invest substantial capital to maintain and upgrade its facilities, including main replacements, treatment plant upgrades and energy efficiency projects. In addition, Kentucky American Water is engaged in a business transformation project regarding the development and

system-wide deployment of new, integrated information technology systems. As part of the business transformation, Kentucky American Water is replacing its antiquated information technology systems that have reached or exceeded the end of their useful lives. The business transformation undertaking will benefit all customers, but is not presently reflected in Kentucky American Water's rates.

4. The cost increases associated with these necessary investments and improvements have not been offset by the additional revenue produced by the increase in rates effective September 28, 2010 in Case No. 2010-00036, which is causing an erosion of earnings for Kentucky American Water as demonstrated in the attached exhibits. Not only are revenues failing to offset the cost increases, Kentucky American Water continues to experience declining usage as a result of increasingly efficient plumbing fixtures and appliances and customer conservation.

5. Kentucky American Water is requesting an increase in rates because its existing rates for water service do not afford Kentucky American Water the opportunity to recover its reasonable operating costs or to earn a just and reasonable rate of return on its investment. Kentucky American Water must be granted a rate increase at this time in order to maintain its facilities and provide service commensurate with its customers' reasonable expectations and the Public Service Commission's requirements, as well as attract capital at reasonable rates. Because Kentucky American Water's present rates do not permit it to fulfill each of these requisites, the rates presently charged are compensatory and are, consequently, unfair, unreasonable, and unjust.

6. As explained in Gary VerDouw's testimony, a concern that must be addressed by many water service providers, including Kentucky American Water, is its aging infrastructure

and the need to replace and/or upgrade its facilities in order to fulfill its obligations of providing safe, adequate, and reliable water service. Because of the substantial capital expenditures that are involved in performing the replacements and/or upgrades, Kentucky American Water is proposing a Distribution System Infrastructure Charge as a tariff rate adjustment mechanism that will allow Kentucky American Water to make capital improvements that will allow safe and reliable service without the frequent filing of rate cases, which will allow customers to gradually absorb the associated costs.

Similarly, Kentucky American Water is also proposing a Purchased Power and Chemicals Charge, which is a tariff rate adjustment mechanism, to recover from or credit to customers the incremental changes in purchased power and chemical costs above or below the level authorized for recovery in a base rate case proceeding through tariffs. Further explanation of the proposed mechanism, and the need for same, is discussed in Mr. VerDouw's testimony.

7. As authorized by KRS 278.192(1) and for the purpose of justifying the reasonableness of the proposed increase in rates, Kentucky American Water has utilized a forward-looking test period corresponding to the first twelve (12) consecutive calendar months the proposed rates will be in effect after the six-month suspension of the proposed rates. The forward-looking test period is the twelve months ending July 31, 2014 (August 1, 2013 – July 31, 2014).

8. Kentucky American Water has used, in the attached exhibits, a base period consisting of the twelve (12) months ending March 31, 2013 (April 1, 2012 – March 31, 2013). This base period begins not more than nine (9) months prior to the date of the filing of this Application, and is a period consisting of not less than six (6) months of historical data and not more than six (6) months of estimated data, all as authorized by KRS 278.192(2)(a).

9. Within forty-five (45) days after the last day of the base period, Kentucky American Water will file the actual results for the estimated months of the base period as required by KRS 278.192(2)(b).

10. Kentucky American Water's annual reports, including the annual report for 2011, are on file with the Public Service Commission as required by 807 KAR 5:006, Section 3(1).

11. Kentucky American Water gives notice to the Public Service Commission of the adjustment of its rates from those set forth in Exhibit No. 1 in the filing requirements to those rates set forth in Exhibit No. 2 in the filing requirements, in the total amount of \$12,317,702 on an annual basis. The percentage increase will approximate an overall increase of 14.64% to Kentucky American Water. A comparison of the current and proposed rates is set forth in attached Exhibit No. 3.

In Case No. 2007-00143, the Public Service Commission approved the implementation of single-tariff pricing for Kentucky American Water. Accordingly, the rates for each customer class are and will be uniform throughout each customer class without regard to Kentucky American Water division. The estimated amount of increase per customer class in both dollars and as a percentage is: residential, \$7,944,541, 17.88%; commercial, \$1,902,961, 8.90%; industrial, \$425,844, 19.83%; private fire hydrants or fire connections, \$231,907, 10.00%; public fire hydrants, \$659,367, 19.71%; municipal and other public authority, \$748,874, 11.84%; and, sales for resale, \$45,796, 2.50%.

The effect upon the average bill for each customer class that the proposed rate change will apply is an increase in the following dollar and percentage amounts: residential, \$5.76, 17.59%; commercial, \$6.79, 3.72%; industrial, \$1,516.35, 18.45%; private fire hydrants and fire

connections, \$7.34, 10.00%; public fire hydrants, \$7.46, 19.71%; municipal and other public authority, \$106.06, 10.92%; and sales for resale, \$362.21, 2.78%.

12. Kentucky American Water is a corporation, and a certified copy of its Articles of Incorporation, together with all amendments, are incorporated by reference as authorized by 807 KAR 5:001, Section 10(1)(b)3 and Section 8(3), and were filed as Filing Exhibit No. 4 in Case No. 95-554, Notice of the Adjustment of The Rates of Kentucky American Water Company Effective on and after February 29, 1996, and are referred to in the attached Exhibit No. 4.

13. Kentucky American Water is a corporation in good standing with the Secretary of State of the Commonwealth of Kentucky. A certificate to that effect, dated within sixty (60) days of December 28, 2012, as required by 807 KAR 5:001, Section 10(1)(b)5, is attached as Exhibit No. 5.

14. The legal name of the applicant is Kentucky-American Water Company. It does business under an assumed name and has filed a Certificate of Assumed Name as required by KRS 365.015. A certified copy of the Certificate of Assumed Name as required by 807 KAR 5:001, Section 10(1)(b)6 is attached as Exhibit No. 6.

15. Kentucky American Water has complied with 807 KAR 5:011, Section 8(2) and 807 KAR 5:001, Section 10(3) and (4), by mailing a typewritten Customer Notice to all customers no later than the date this Application, Statement and Notice was filed with the Public Service Commission and by posting a sample copy of the Customer Notice at its principal office and place of business in each division no later than the date this Application, Statement and Notice was filed with the Public Service Commission. A copy of the Customer Notice is attached as Exhibit No. 7.

16. Kentucky American Water has filed with the Executive Director of the Public Service Commission a written notice of its intention to file this rate application. The notice stated that the application would be supported by a fully forecasted test period, was delivered to the Executive Director's office on November 29, 2012 and a copy was provided to the Utility Intervention and Rate Division of the Attorney General's office of the Commonwealth of Kentucky as required by 807 KAR 5:001, Section 10(2) and 807 KAR 5:011, Section 8(1). A copy of the notice is attached as Exhibit No. 8.

17. As required by 807 KAR 5:001, Section 10(4)(f), Kentucky American Water will post a copy of Exhibit No. 7 of the filing requirements at its places of business on December 28, 2012, and it will remain posted until the Public Service Commission has finally determined Kentucky American Water's rates.

18. In support of its application for a general adjustment of rates, supported by a fully forecasted test year, Kentucky American Water has presented its financial data for the forecasted period in the form of pro forma adjustments to the base period, has limited the forecasted adjustments to the twelve (12) calendar months immediately following the suspension period, and has based capitalization and net investment rate base on a thirteen (13) month average for the forecasted period, all as set forth in 807 KAR 5:001, Section 10(8)(a)(b) and (c), in Exhibits No. 37B, 37D and 37J.

19. In further support of its application for a general adjustment of rates, supported by a fully forecasted test year, Kentucky American Water attaches the following documents or explains their absence:

Filing Requirements	Abbreviated Document Description	Location or Absence Reason
807 KAR 5:001 Section 10(8)(f)	Rate base/capital reconciliation	Exhibit 9
807 KAR 5:001 Section 10(9)(a)	Testimony of Witnesses - Jermaine K. Bates - Linda C. Bridwell - Keith L. Cartier - Paul R. Herbert - Lewis E. Keathley - Cheryl D. Norton - Scott W. Rungren - Melissa L. Schwarzell - Dr. James H. Vander Weide - Gary M. VerDouw - Lance E. Williams	Exhibit 10
807 KAR 5:001 Section 10(9)(b)	Capital construction budget with a 3-year forecast	Exhibit 11
807 KAR 5:001 Section 10(9)(c)	Description of forecast factors	Exhibit 12
807 KAR 5:001 Section 10(9)(d)	Annual and monthly budget for 12 months preceding 12/28/12, the base period and the forecasted period	Exhibit 13
807 KAR 5:001 Section 10(9)(e)	Cheryl D. Norton's statement of attestation	Exhibit 14
807 KAR 5:001 Section 10(9)(f)	Information about major construction projects	Exhibit 15
807 KAR 5:001 Section 10(9)(g)	Information about other construction projects	Exhibit 16

807 KAR 5:001 Section 10(9)(h)1	Financial forecast for the capital construction forecasted years - operating income statement	Exhibit 17
807 KAR 5:001 Section 10(9)(h)2	Financial forecast for the capital construction forecasted years - balance sheet	Exhibit 18
807 KAR 5:001 Section 10(9)(h)3	Financial forecast for the capital construction forecasted years - cash flow statement	Exhibit 19
807 KAR 5:001 Section 10(9)(h)4	Financial forecast for the capital construction forecasted years - revenue requirements	Exhibit 20
807 KAR 5:001 Section 10(9)(h)5	Financial forecast - energy and demand load forecast	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(h)6	Financial forecast - access line forecast	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(h)7	Financial forecast - generation mix	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(h)8	Financial forecast - gas supply mix	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(h)9	Financial forecast for the capital construction forecasted years - employee level	Exhibit 21
807 KAR 5:001 Section 10(9)(h)10	Financial forecast for the capital construction forecasted years - labor cost changes	Exhibit 22
807 KAR 5:001 Section 10(9)(h)11	Financial forecast for the capital construction forecasted years - capital structure requirements	Exhibit 23

807 KAR 5:001 Section 10(9)(h)12	Financial forecast for the capital construction forecasted years - rate base	Exhibit 24
807 KAR 5:001 Section 10(9)(h)13	Financial forecast for the capital construction forecasted years - water sales (gallons)	Exhibit 25
807 KAR 5:001 Section 10(9)(h)14	Financial forecast for the capital construction forecasted years - customer forecast	Exhibit 26
807 KAR 5:001 Section 10(9)(h)15	Financial forecast - gas sales forecast	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(h)16	Financial forecast - toll and access forecast	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(i)	FERC or FCC audit reports	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(j)	Most recent stock or bond prospectus	Exhibit 27
807 KAR 5:001 Section 10(9)(k)	FERC 1, FERC 2, ARMISR and PSCT	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(l)	Annual reports to shareholders, most recent five years	Exhibit 28
807 KAR 5:001 Section 10(9)(m)	Current chart of accounts	Exhibit 29
807 KAR 5:001 Section 10(9)(n)	Latest 12 monthly managerial reports	Exhibit 30
807 KAR 5:001 Section 10(9)(o)	Monthly budget variance reports for 12 months pre-base period, for base period, and subsequent months as available	Exhibit 31
807 KAR 5:001 Section 10(9)(p)	SEC 10-Ks, 8-Ks and 10-Qs	Not required of Kentucky American Water
807 KAR 5:001 Section 10(9)(q)	Independent auditor's annual opinion report and any written findings of material weaknesses in internal controls	Exhibit 32 There is no finding of material weaknesses.

807 KAR 5:001 Section 10(9)(r)	Quarterly reports to shareholders	Kentucky American Water does not issue quarterly reports to shareholders.
807 KAR 5:001 Section 10(9)(s)	Summary of last depreciation study	Exhibit 33
807 KAR 5:001 Section 10(9)(t)	List of software, programs and models used	Exhibit 34
807 KAR 5:001 Section 10(9)(u)	Affiliate, general or home office allocations	Exhibit 35
807 KAR 5:001 Section 10(9)(v)	Cost of service study	Exhibit 36
807 KAR 5:001 Section 10(9)(w)	Cost of service study for local exchange carriers	Inapplicable to a water company
807 KAR 5:001 Section 10(10)(a)	Jurisdictional financial summary for the base and forecasted period	Exhibit 37, Schedule A
807 KAR 5:001 Section 10(10)(b)	Jurisdictional rate base summary for the base and forecasted period	Exhibit 37, Schedule B
807 KAR 5:001 Section 10(10)(c)	Jurisdictional operating income summary for base and forecasted period	Exhibit 37, Schedule C
807 KAR 5:001 Section 10(10)(d)	Jurisdictional adjustment to operating income	Exhibit 37, Schedule D
807 KAR 5:001 Section 10(10)(e)	Jurisdictional federal and state income tax summary for base and forecasted period	Exhibit 37, Schedule E
807 KAR 5:001 Section 10(10)(f)	Organizational membership dues, initiation fees, country club expenditures, charitable contributions, marketing expenses, sales expenses, advertising expenses, professional service expenses, civic and political activity expenses, employee parties and outings expenses, employee gift expenses, and rate case expenses for the base and forecasted periods	Exhibit 37, Schedule F
807 KAR 5:001 Section 10(10)(g)	Payroll costs analysis	Exhibit 37, Schedule G

807 KAR 5:001 Section 10(10)(h)	Computation of gross revenue conversation factor	Exhibit 37, Schedule H
807 KAR 5:001 Section 10(10)(i)	Comparative income statements, revenue statistics and sales statistics for five most recent calendar years, the base period, forecasted period and two calendar years beyond the forecast period	Exhibit 37, Schedule I
807 KAR 5:001 Section 10(10)(j)	Cost of capital summary for base period and forecasted period	Exhibit 37, Schedule J
807 KAR 5:001 Section 10(10)(k)	Comparative financial data and earning measures for the ten most recent calendar years, base period and forecasted period	Exhibit 37, Schedule K
807 KAR 5:001 Section 10(10)(l)	Narrative description and explanation of all proposed tariff changes	Exhibit 37, Schedule L
807 KAR 5:001 Section 10(10)(m)	Revenue summary for base period and forecasted period with detailed billing analysis for all customer classes	Exhibit 37, Schedule M
807 KAR 5:001 Section 10(10)(n)	Typical bill comparison under present and proposed rates for all customer classes	Exhibit 37, Schedule N

This Application, Statement and Notice is filed under the provisions of KRS 278.180 and 278.190, and the Public Service Commission is requested to find the proposed rates to be fair, just and reasonable under KRS 278.030(1).

KENTUCKY-AMERICAN WATER COMPANY

BY: Cheryl D. Norton
Cheryl D. Norton, President

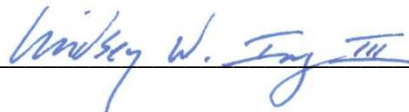
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CERTIFICATE

In accordance with Ordering Paragraph No. 10 of the Commission's December 17, 2012 Order, this is to certify that Kentucky-American Water Company's December 28, 2012 electronic filing is a true and accurate copy of the documents to be filed in paper medium; that the electronic filing has been transmitted to the Commission on December 28, 2012; that an original and one copy of the filing will be delivered to the Commission on December 28, 2012; and that no party has been excused from participation by electronic means.

STOLL KEENON OGDEN PLLC

By 

Attorneys for Kentucky-American Water Company