

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF	)	
BLUEGRASS WATER UTILITY OPERATING	)	CASE NO.
COMPANY, LLC FOR AN ADJUSTMENT OF	)	2020-00290
RATES AND APPROVAL OF	)	
CONSTRUCTION	)	

ORDER

This matter arises from an application for a rate increase and approval of construction filed by Bluegrass Water Utility Operating Company, LLC (Bluegrass Water) pursuant to KRS 278.020(1), KRS 278.180, and KRS 278.190. The Kentucky Attorney General, through the Office of Rate Intervention (Attorney General) and a number of groups representing Bluegrass Water’s customers (collectively, Joint Intervenors)<sup>1</sup> were permitted to intervene in this matter. Bluegrass Water responded to requests for information from the Attorney General, Joint Intervenors, and Commission Staff, and a hearing was conducted in this matter on May 18, 2021, through May 20, 2021. Bluegrass Water responded to post-hearing request for information and Joint Intervenors and the Attorney General filed post-hearing briefs, and Bluegrass Water filed a brief in response to intervenors’ post-hearing briefs. This matter is now before the Commission for a decision on the merits.

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<sup>1</sup> The groups representing Bluegrass Water’s customers are Homestead Home Owners Association, Inc.; The Deer Run Estates Homeowners Association, Inc.; Longview Homeowners Association, Inc.; Arcadia Pines Sewer Association, Inc., Carriage Park Neighborhood Association, Inc., Marshall Ridge Sewer Association, Inc. and Randview Septic Corporation. They are all represented by the same counsel and have therefore acted collectively in the proceedings before the Commission. Thus, the Commission refers to them collectively as Joint Intervenors.

## BACKGROUND

Bluegrass Water is a limited liability company organized under the laws of Kentucky on March 21, 2019. Beginning in April 2019, Bluegrass Water began filing applications pursuant to KRS Chapter 278 to purchase water and wastewater systems in Kentucky. On August 14, 2019, Bluegrass Water was approved to purchase the Airview Utilities, LLC (Airview), Brocklyn Utilities, LLC (Brocklyn), Fox Run Utilities, LLC (Fox Run), Marshall County Environmental Services, LLC (Great Oaks and Golden Acres), Kingswood Development, Inc. (Kingswood), Lake Columbia Utilities, Inc. (Lake Columbia), LH Treatment Company, LLC (Longview/Homestead), and P.R Wastewater Management, Inc (Persimmon Ridge) wastewater systems in Hardin, Madison, Franklin McCracken, Marshall, Bullitt, Scott, and Shelby counties.<sup>2</sup> On February 17, 2020, Bluegrass Water was approved to purchase the River Bluffs, Inc. (River Bluffs) and Joann Estates Utilities, Inc. (Timberland) wastewater systems in Oldham and McCracken counties and the Center Ridge Water District, Inc. (Center Ridge) water systems in Calloway County.<sup>3</sup> On June 19, 2020, Bluegrass Water was approved to purchase the Arcadia Pines Sewer Association, Inc. (Arcadia Pines), Carriage Park Neighborhood Association Inc. (Carriage Park), Marshall Ridge Sewer Association Inc. (Marshall Ridge), and Randview Septic Corporation (Randview) wastewater systems in McCracken and

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<sup>2</sup> Case No. 2019-00104, *Electronic Proposed Acquisition by Bluegrass Water Utility Operating Company, LLC and the Transfer of Ownership and Control of Assets by P.R. Wastewater Management, Inc., Marshall County Environmental Services, LLC, LH Treatment Company, LLC, Kingswood Development, Inc., Airview Utilities, LLC, Brocklyn Utilities, LLC, Fox Run Utilities, LLC, and Lake Columbia Utilities, Inc.* (Ky. PSC Feb. 25, 2021).

<sup>3</sup> Case No. 2019-00360, *Electronic Proposed Acquisition by Bluegrass Water Utility Operating Company, LLC and the Transfer of Ownership and Control of Assets by Center Ridge Water District, Inc., Joann Estates Utilities, Inc., and River Bluffs, Inc.* (Ky. PSC Feb. 17, 2020).

Graves counties.<sup>4</sup> On January 14, 2021, Bluegrass Water was approved to purchase the Delaplain Disposal Company (Delaplain), Herrington Haven Wastewater Company Inc. (Herrington Haven), Springcrest Sewer Company, Inc. (Springcrest), and Woodland Acres Utilities, LLC (Woodland Acres) wastewater systems in Scott, Garrard, Jessamine, and Bullitt counties. Bluegrass Water is categorized as a class B sewer utility and a class C water utility.

Bluegrass Water tendered its application in this matter on October 1, 2020.<sup>5</sup> However, on October 30, 2020, Bluegrass Water was sent a deficiency letter that identified information required by 807 KAR 5:001, Section 16 that was not provided with the application. On the same day, the Commission issued an Order noting the same deficiencies issued in the letter and stating that Bluegrass Water must cure those deficiencies as directed in the deficiency letter before the application may be accepted for filing. In the October 30, 2020 Order, the Commission also noted that Bluegrass Water had not closed on the Arcadia Pines, Carriage Park, Marshall Ridge, and Randview wastewater systems when it tendered the application and explicitly stated that Bluegrass Water must close on those systems before it cures the deficiencies identified in the letter and the application is accepted for filing if it wanted the application to be considered a request for a rate adjustment for those systems. On November 19, 2020, Bluegrass Water closed on the Arcadia Pines, Carriage Park, Marshall Ridge, and Randview

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<sup>4</sup> Case No. 2020-00028, *Electronic Proposed Acquisition by Bluegrass Water Utility Operating Company, LLC of Wastewater System Facilities and Subsequent Tariffed Service to Users Presently Served by those Facilities* (Ky. PSC Jun. 19, 2020).

<sup>5</sup> Note that Bluegrass Water tendered some of the attachments to the application on September 30, 2020 and tendered the application itself on September 30, 2020 in Case No. 2020-00297. Bluegrass Water corrected that issue and tendered the application in this matter on October 1, 2020.

wastewater systems and cured the filing deficiencies identified in the October 30, 2020 letter. Bluegrass Water's application was deemed to have been filed on November 19, 2020.

However, as of November 19, 2020, Bluegrass Water had not been approved to purchase and did not own the systems for which it sought approval to purchase in Case No. 2020-00297; the Delaplain, Herrington Haven, Springcrest, and Woodland Acres sewer systems (the 00297 systems). The Commission denied Bluegrass Water's request for a deviation from 807 KAR 5:011, Section 11, and determined that, pursuant to 807 KAR 5:011, Section 11, and KRS Chapter 278, Bluegrass Water could not file a tariff proposing to increase the rates of the 00297 systems until it completed the purchase of those systems and adopted the existing tariffs of those systems. Thus, the Commission held that Bluegrass Water's application in this matter, which was filed before Bluegrass Water was even approved to purchase those systems, would not be considered as a request to increase the rates of the 00297 systems pursuant to KRS Chapter 278.

Bluegrass Water's application proposes a rate increase based on a forecasted test period ending April 30, 2022, and requests rates based on a total revenue requirement for water and sewer customers of \$3,758,757. Bluegrass Water indicated that revenue requirement represents an increase of \$2,513,799 over projected revenues derived from current rates for the systems Bluegrass Water owns and operates and the systems it was seeking to operate when it tendered its application. The total proposed revenue requirement consists of a revenue requirement for sewer of \$3,332,039.61, including the costs associated with the 00297 systems, and a revenue requirement for water of \$426,747. If Bluegrass Water collected its total proposed revenue requirement of

\$3,758,757, the rates of its systems would need to be increased by about approximately 200 percent.

Bluegrass Water filed tariff sheets with its application that included a proposed flat, unified rate for residential sewage customers of \$96.14 per month and a proposed flat unified rate for residential water customers of \$105.84 per month. Bluegrass Water's customers are currently served under separate distinct rates based on the systems that provide them service, which are based on the filed rates or the amounts charged by the previous owners of the systems. Bluegrass Water indicated that residential customers of the sewer systems at issue currently pay flat rates ranging from \$15.00 to \$55.85 per month such that the proposed rate of \$96.14 per month will represent a 72.1 percent to a 540.9 percent increase in residential rates. Bluegrass Water indicated that residential customers of water systems at issue currently pay a flat rate of \$22.79 per month such that the proposed rate of \$105.84 per month will represent a 364.4 percent increase in those residential rates.

Bluegrass Water, in support of its application, presented schedules and written testimony from Josiah Cox, Todd Thomas, Jacob Freeman, Brent Thies, Dylan D'Ascendis, and Jennifer Nelson. Among other things, Bluegrass Water indicated that the proposed rates are necessary in large part due to the significant capital investment Bluegrass Water has or will make through the forecasted test period. Bluegrass Water asserted that it has made or that it will be necessary to make about \$4.39 million in capital investments in the sewage systems at issue, about \$1.16 million in capital investments in the water systems at issue, and about \$2.01 million in capital investments in the 00297

systems.<sup>6</sup> In its application, Bluegrass Water contended that a Certificate of Public Convenience and Necessity (CPCN) was not required for the projects but alternatively requested a CPCN for any project for a CPCN would be required.

On June 30, 2021, Bluegrass Water filed a notice of intent to implement its proposed rates, which were suspended in a previous Commission Order, on August 1, 2021, pending the final Order and subject to refund as required by KRS 278.190. However, although Bluegrass Water indicated it maintained its objections, it indicated it would not implement any new rate, subject to refund, for the 00297 systems, which it did not own at the time this application was filed.

### MISCELLANEOUS ISSUES

#### Rates of Systems at Issue in Case No. 2020-00028

Joint Intervenors argue that the Commission should reject Bluegrass Water's request for a rate increase with respect to the four systems Bluegrass Water was approved to purchase in Case No. 2020-00028, which are Arcadia Pines, Carriage Park, Marshall Ridge, and Randview (collectively, the 00028 systems). Joint Intervenors note that Bluegrass Water closed on those systems the same day its application was accepted for filing in this matter. Joint Intervenors argue that Bluegrass Water could not file a rate application based on a forecasted test period for those customers, because KRS 278.192 requires six months of actual historical data to support a rate case based on a forecasted test period. Joint Intervenors also argue that Bluegrass Water, in its application in Case No. 2020-00028, committed to waiting to file for a rate increase for those systems until

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<sup>6</sup> See *generally* Application, Exhibit 8, Direct Testimony of Jacob Freeman (Freeman Testimony).

Bluegrass Water had one year of historical data from owning and operating those systems.<sup>7</sup>

Bluegrass Water disputes Joint Intervenors' interpretation of KRS 278.192. It notes that it had more than six months of historical data from operations when it filed its application in this matter. Bluegrass Water argues that information is sufficient to comply with KRS 278.192, even though it did not have six months of historical data for the 00028 systems. Bluegrass Water also disputes that it committed not to increase the rates of the 00028 systems for a year in its application in Case No. 2020-00028. Bluegrass Water argues that the issue in Case No. 2020-00028 was that the systems were not being operated as rate-regulated utilities by the former owners such that there was no tariff on file for Bluegrass Water to adopt pursuant to 807 KAR 5:011 and insufficient information to establish rates pursuant to 807 KAR 5:076.<sup>8</sup> Bluegrass Water stated that it proposed initial rates for the 00028 systems based on the amounts charged by the current owners and that it then "committed" to apply for a rate adjustment for those systems "no later than 15 months after their acquisition."<sup>9</sup> Bluegrass Water also notes that it indicated it would file such an application "by mid-2021." Bluegrass Water argues that intervenors are incorrect in stating that "Bluegrass 'originally indicated' (AG Brief. p.7) or made an 'express commitment' or 'regulatory commitment' (Jt. Int. Brief pp. 5-6) to wait until mid-

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<sup>7</sup> Joint Intervenors' Post-Hearing Brief (Joint Intervenors' Brief) (filed June 3, 2021) at 5-7.

<sup>8</sup> Bluegrass Water's Post-Hearing Response Brief (Bluegrass Water Response Brief)(filed June 9, 2021) at 3.

<sup>9</sup> *Id.* at 4.

2021 to file for an adjustment of rates for the 00028 systems or state-wide.”<sup>10</sup> Bluegrass Water also argues that the Commission’s final Order in Case No. 2020-00028 did not explicitly condition approval of the transfers on Bluegrass Water agreeing to wait until mid-2021 to apply for a rate increase.<sup>11</sup>

If the Commission accepted Joint Intervenors’ argument with respect to the interpretation of KRS 278.192, it would essentially be holding that KRS 278.192 prevents a utility from including the customers of a system it purchased within six months in an application for a rate increase based on a forecasted test period. The Commission does not believe that such an interpretation is supported by the plain reading of the statute. Further, there was no explicit commitment or condition in Case No. 2020-00028 requiring Bluegrass Water to wait to file for a rate increase for the 00028 systems. Thus, the Commission finds no reason that Joint Intervenors’ request that the Commission reject the proposed rate increase as it pertains to the 00028 systems should be granted.

However, the Commission notes that when a utility files an application for a rate increase that “the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the utility.”<sup>12</sup> If a utility includes a new system without accurate historical data, then it may be unable to meet its burden, and the Commission may reject or reduce the proposed rate as appropriate.

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<sup>10</sup> *Id.*

<sup>11</sup> *Id.*

<sup>12</sup> KRS 278.190.

## Rates of Systems at Issue in Case No. 2019-00104

Joint Intervenors argue that Bluegrass Water broke an additional commitment to the Commission by filing a rate case using a forecasted test year for the systems acquired in Case No. 2019-00104 (the 00104 systems), because Josiah Cox, President of Bluegrass Water, had testified at a hearing in Case No. 2019-00104 that its first rate filing would be based upon the company's "current expenses." Joint Intervenors argue that Bluegrass Water seeks to inject millions of dollars of additional rate base and operation and maintenance expense into its revenue requirement. Joint Intervenors argue that Bluegrass Water should not be able to use a forecasted test year based on its commitment to use "current expenses."

Bluegrass Water responded that Mr. Cox, after explaining that "historical information is not necessarily informative," answered a question regarding a timeline for seeking a unified rate by stating: "[W]e would run the systems for some period of time before we would come back and apply for a unified rate based on what our current costs are."<sup>13</sup> Bluegrass Water argued that in context the statement is to distinguish such a rate filing from one based on the past owners historical expenses. Further, Bluegrass Water claims that this current rate case is based on its current expenses, due to the inclusion of 2020 base year actuals.<sup>14</sup> Bluegrass Water argues that there is no justification for prohibiting a rate adjustment through use of a forecasted test year from including the 00104 systems.

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<sup>13</sup> Bluegrass Water's Response Brief at 4, footnote 4.

<sup>14</sup> *Id.*

The Commission agrees with Bluegrass Water that the statement made by Mr. Cox at the hearing in Case No. 2019-00104 would not prohibit Bluegrass Water from filing a rate adjustment based on a forecasted test year that included the 00104 systems. Given the context of the statement, it was not an explicit commitment to file a rate case based on a historical test year. Further, KRS 278.192 allows Bluegrass Water to apply for a rate increase based on a forecasted test year for the systems at issue in Case No. 2019-00104, and Joint Intervenors have not provided any basis for finding that the statute would not apply under the circumstances. Thus, the Commission finds that the Joint Intervenors' request that the proposed rate increase be dismissed for the 00104 systems or that rates be limited to purely historical information for those systems should not be granted.<sup>15</sup>

#### Exclusion of Systems at Issue in Case No. 2020-00297

Joint Intervenors argue that the Commission correctly found, in a February 12, 2021 Order, that Bluegrass Water had not adopted the tariffs of the 00297 systems when it filed the application in this matter and, therefore, that Bluegrass Water could not apply for a rate increase for the customers of those systems as part of this application. Joint Intervenors further argue that all proposed capital investments for the systems acquired in Case No. 2020-00297 be removed for ratemaking purposes in this proceeding.<sup>16</sup> Joint Intervenors point out that the systems in question were not owned by Bluegrass Water at the time the application for the current proceeding was tendered and state that there is

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<sup>15</sup> The Commission also notes that even if it limited the 00104 systems to a historical test period that Bluegrass Water would be able to project known and measurable changes.

<sup>16</sup> Joint Intervenors' Brief at 4.

no precedent for a Kentucky utility utilizing a forecast test year to raise rates on customers of a system that it does not yet own.<sup>17</sup>

Joint Intervenors also argue that exclusion of the plant for the 00297 systems is justified by the “used and useful” doctrine. Specifically, Joint Intervenors assert that the systems owned by Bluegrass Water do not draw service from a centralized source and operate independently of one another such that capital expenditures made to rehabilitate one system will never benefit the customers of another system. Thus, Joint Intervenors argue that the sharing of these costs across systems is unjust.<sup>18</sup>

Bluegrass Water states that it based its application for an adjustment of rates on a fully forecasted test year ending April 30, 2022. Bluegrass Water indicated that it proposed a unified rate for all systems forecast to be owned and operated by Bluegrass Water during the forecasted test period. Bluegrass Water asserts that it in fact does now own the 00297 systems as forecasted. Bluegrass Water noted that it disputes the Commission’s order to exclude the 00297 systems from the rate adjustment, “but here neither waives nor repeats arguments against exclusion.”<sup>19</sup>

Bluegrass Water contends that Joint Intervenors’ attempt to revisit the decision to exclude the 00297 systems advances “tendentious arguments purportedly in support of the Commission’s decision, most notably a radical position that costs for necessary investment in treatment or collection/distribution infrastructure cannot be recovered from

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<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> Bluegrass Water’s Response Brief at 2–3.

‘consumers who will never benefit from them.’”<sup>20</sup> Bluegrass Water asserts that the rule proposed by Joint Intervenors would require individualized rates for each service location. Bluegrass Water notes that such a rule is violated each time rates are set and gave the example of a rate for a long established electric customer that includes the cost to construct new transmission and distribution lines to extend the service area or a reach new residential, commercial, or industrial development. Bluegrass Water argues that “[n]either law nor policy supports atomizing rates or de-averaging based on the nearest facilities and how close the customer is to them.”<sup>21</sup>

As an initial matter, for the reasons expressed in previous orders, the Commission sees no reason to reconsider its previous decisions in the February 12, 2021 Order and the March 24, 2021 Order on reconsideration denying Bluegrass Water’s request for a deviation and finding that Bluegrass Water must first adopt the existing tariffs of the utilities at issue in Case No. 2020-00297, pursuant to 807 KAR 5:011, Section 11, before filing a tariff proposing to increase rates for those systems, pursuant the 807 KAR Chapter 5 and KRS Chapter 278, with 30 days’ notice to the Commission.<sup>22</sup> Further, as the Commission noted in the orders addressing that issue, Bluegrass Water is proposing to combine the separate rates of multiple systems into a single rate in this matter and,

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<sup>20</sup> *Id.* at 2.

<sup>21</sup> *Id.*

<sup>22</sup> The Commission observes that Bluegrass Water adopted the tariffs of the previous utilities at the end of March 2021 and that in April 2021 Bluegrass Water filed tariffs bringing those systems within its tariff, which included separate rate sheets for each of those systems, consistent with the rate sheets it attached as an exhibit in Case No. 2020-00297 and indicated it would file, setting rates for those systems at the same level as the previous owner. Bluegrass Water has filed no new tariff sheets proposing to increase the rates of those or any other systems since those tariffs were filed.

therefore, the Commission would be looking at the costs attributable to each system separately, even if the Commission ultimately adopted a unified rate for the systems at issue in this case, when reviewing whether the proposed rates were reasonable.<sup>23</sup> The issue raised by Joint Intervenors is, in part, whether it is reasonable to include costs attributable to separate systems that are not included in a unified rate.

While the Commission, as discussed herein, is approving a unified rate for the systems at issue in this case, the Commission finds that it is not reasonable to include the costs of systems not included here among the costs that would be recovered from other customers. As discussed in more detail below, there are reasons for approving a unified rate as opposed to a single rate for each system, including that a unified rate is likely to promote regionalization, which should drive down costs in the long term by allowing utilities to take advantage of economies of scale, and that a unified rate will serve to levelize rates in the long term so that each system will not experience a significant rate shock every time it requires significant investment or some unexpected cost, which all systems will experience at some point. However, such cost sharing is not reasonable where the customers of a distinct system with wholly separate rates is not included in the unified rate. Thus, the Commission finds that the costs associated with the 00297 systems should not be included in establishing the revenue requirement for a unified rate in this matter and that they should be treated as distinct systems, whose rates are not at issue, for the purpose of setting rates for systems at issue in this matter.<sup>24</sup>

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<sup>23</sup> See Order (Ky. PSC Mar. 24, 2021) at 8–9.

<sup>24</sup> As Bluegrass Water noted, the inclusion of the 00297 systems in the unified rate would have actually lowered the overall rate.

As discussed in more detail below, the Commission will remove all capital costs associated with the 00297 systems when determining the revenue requirement for the systems at issue in this matter. Similarly, the Commission finds that operating revenues and expenses associated with the 00297 systems should be removed.

#### Governance and Accountability

Joint Intervenors assert that Bluegrass Water's Operating Agreement allows its sole member, CSWR, LLC (CSWR), to reorder the priority of making both regular and capital distributions and distributions upon the dissolution of the company. Joint Intervenors argue that "the governing documents expressly permit CSWR to take advantage of Bluegrass Water and, by extension, their customers," though Joint Intervenors acknowledge that it is probably unlikely to happen.<sup>25</sup>

While Joint Intervenors are not specific, they appear to be concerned that Bluegrass Water would make payments to CSWR before making payments to creditors or contractors. The Commission notes that Bluegrass Water already has a statutory obligation to provide adequate service to customers and that Bluegrass Water is prohibited from transferring utility assets without prior Commission approval. The Commission does not believe that additional conditions are appropriate at this time, though it may revisit imposing conditions, pursuant to KRS 278.300, on the order of payment when Bluegrass Water applies for financing approval.

#### Procedural Issues

Bluegrass Water tendered a document titled "Statement of Non Existence/ Inapplicability of Certain Rate-Application Requirements or, in the alternative, Request

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<sup>25</sup> Joint Intervenors' Brief at 25.

for Waiver of Requirement(s)” with its application in this matter. At the hearing in this matter, Bluegrass Water identified this document as a motion on which the Commission had not yet ruled. However, the requirements either were satisfied by the information or explanation provided or were not applicable to this case.<sup>26</sup> Further, the document was not clear that it was intended to be a motion filed pursuant to 807 KAR 5:001 in the event the Commission found that no waiver from the filing requirements was necessary, and no deficiency relevant to filing requirements mentioned was identified. Thus, the Commission finds that there is no need to take any action on this document.

Bluegrass Water also filed a motion for an enlargement of time to respond to Commission Staff’s Third Request for Information. Specifically, responses to the requests were due on March 22, 2021, and Bluegrass Water partially responded on that date, but noted that it was still compiling information to respond to additional requests for information and requested until March 26, 2021, to provide that information. Having reviewed that motion and being otherwise sufficiently advised, the Commission will grant that motion as it indicated it would at the hearing in this matter.

#### CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY

##### Bluegrass Water and Intervenors’ Positions

Bluegrass Water indicated in its application that it planned projects, itemized in the testimony of Jacob Freeman, to repair, replace, and improve the sewer and water facilities

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<sup>26</sup> See 807 KAR 5:001, Section 16(7) (indicating that a utility should provide the explanation “or a statement explaining why the required information does not exist and is not applicable to the utility’s application”).

it owns and operates or was approved or requested approval to own and operate.<sup>27</sup> Bluegrass Water acknowledged in testimony and other filings made with its application that it had started some of the projects when it filed its application.<sup>28</sup> Bluegrass Water argued that most of its projects are needed to maintain capacity and basic functionality of the systems or to achieve compliance with environmental regulations, and that other projects will achieve operational efficiencies as well as enhance the present quality of service for Bluegrass Water's customers.<sup>29</sup>

Bluegrass Water asserted in its application that “[a]ll or most of the individual projects would not be categorized as new construction or extensions for which a [CPCN] is needed.”<sup>30</sup> Bluegrass Water argued that the projects do not extend the Bluegrass Water service area, do not create a wasteful duplication, or conflict with the service offered by other utilities.<sup>31</sup> Bluegrass Water requested a finding that a CPCN is not needed for any one of the projects or, in the alternative, Bluegrass Water requests a CPCN for any projects that are found to be subject to the requirement that a CPCN be obtained.<sup>32</sup>

At the hearing, Josiah Cox, Bluegrass Water's President, testified that he felt a CPCN would be necessary if the project involved the construction of a new tank or

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<sup>27</sup> Application at 11.

<sup>28</sup> Response to Attorney General's Post-Hearing Requests, Item 1, AG\_post-hearing\_DR01.xlsx (indicating the amounts spent on each of the projects identified in Mr. Freeman's testimony to date).

<sup>29</sup> Application at 14.

<sup>30</sup> Application at 11–12.

<sup>31</sup> Application at 12.

<sup>32</sup> Application at 12.

process.<sup>33</sup> He said that he identified a number of projects that had not been completed that he felt met that criteria and, therefore, would require a CPCN. Specifically, he indicated that he believed the following projects would require a CPCN:

1. The addition of a flow equalization tank at Airview;
2. The construction of a new plant at Brocklyn;
3. The addition of flow equalization and a sludge digester at Fox Run;
4. The addition of a sludge digester at Lake Columbia;
5. The addition of a moving bed bioreactor at Permission Ridge;
6. The conversion of the plant at Delaplain to a moving bed bioreactor to increase the capacity of the plant and the addition of a strainer;
7. The addition of a moving bed bioreactor at Herrington Haven; and
8. The conversion of the Woodland Acres systems to a moving bed bioreactor.<sup>34</sup>

Joint Intervenors argue that Bluegrass Water overlooked the requirement that a project must “not involve sufficient capital outlay to materially affect the existing financial condition of the utility involved” or “result in increased charges to its customers” when arguing that a CPCN is not necessary.<sup>35</sup> Joint Intervenors, referring to Mr. Cox’s testimony, contend that Bluegrass Water acknowledged that the capital projects are material to its financial condition and will result in a rate increase.<sup>36</sup> They also assert that

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<sup>33</sup> May 19, 2021 Hearing Video Transcript (H.V.T.) at 09:41:40.

<sup>34</sup> May 19, 2021 H.V.T. at 09:39:51-09:41:40.

<sup>35</sup> Joint Intervenors’ Brief at 20.

<sup>36</sup> Joint Intervenors’ Brief at 21.

it is not credible for Bluegrass Water to argue that its actual construction projects to date did not require a CPCN given the level of spending Bluegrass Water proposed and has completed.<sup>37</sup> Joint Intervenors further argue that Bluegrass Water made structural improvements and replaced major components of its newly acquired systems.<sup>38</sup> Thus, Joint Intervenors argue Bluegrass Water's projects do not qualify as extensions of existing systems in the usual course of business and, therefore, that a CPCN is required for all of the projects proposed by Bluegrass Water.<sup>39</sup>

Joint Intervenors next argue that no CPCN should be awarded for additional capital investment until Bluegrass Water certifies the actions it has taken to explore reasonable alternatives. Joint Intervenors assert that when pressed about reasonable alternatives to proposed projects that Bluegrass Water could not provide details on what connections to other systems might be available or when discussions regarding additional available connections might take place. Joint Intervenors state, referring to Bluegrass Water's response to post-hearing data requests, that the projects for which Bluegrass Water requests a CPCN are all systems within one mile of other systems. Joint Intervenors contend that Bluegrass Water has not established that its projects are the reasonable, least cost alternatives. Joint Intervenors argue that the Commission should either (1) deny the request for CPCNs or further capital investment for these systems without

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<sup>37</sup> Joint Intervenors' Brief at 21–23.

<sup>38</sup> Joint Intervenors' Brief at 23 (citing May 18, 2021 H.V.T. 14:04:30–14:40:30).

<sup>39</sup> Joint Intervenors' Brief at 23.

prejudice; or (2) keep this portion of Bluegrass’s case open and pending for further action following the entry of a rate order within the suspension period.<sup>40</sup>

The Attorney General argues that the Commission should scrutinize each of Bluegrass Water’s capital projects to ensure that all construction projects undertaken by Bluegrass Water are in furtherance of maintaining only basic functionality of each system and ensure that wasteful gold plating of the systems does not occur. The Attorney General specifically questions the Mission alarm installation and remote monitoring proposed in the application. The Attorney General notes that to comply 807 KAR 5:071(7)(4), Bluegrass Water’s contractors will need to visit the systems daily to inspect all mechanical equipment. The Attorney General argues that remote monitoring may constitute unnecessary duplication of service if contractors will be physically present at each system daily and that such wasteful duplication should be denied.<sup>41</sup>

#### Discussion of When a CPCN is Required

KRS 278.020(1)(a) generally requires a utility to obtain a CPCN before beginning the construction of any plant, equipment, property, or facility for furnishing to the public any utility, including water and sewer service. However, a CPCN is not required for “ordinary extensions of existing systems in the usual course of business.”<sup>42</sup> An “ordinary extension . . . in the usual course of business” is not defined in KRS 278.020 or elsewhere

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<sup>40</sup> Joint Intervenors’ Brief at 23–24.

<sup>41</sup> Attorney General’s Post-Hearing Brief (AG’s Brief)(filed June 3, 2021) at 3–4.

<sup>42</sup> KRS 278.020(1)(a)1.

in KRS Chapter 278. For that reason, the Commission promulgated 807 KAR 5:001, Section 15(3),<sup>43</sup> which states:

Extensions in the ordinary course of business. A certificate of public convenience and necessity shall not be required for extensions that do not create wasteful duplication of plant, equipment, property, or facilities, or conflict with the existing certificates or service of other utilities operating in the same area . . . . , *and* that do not involve sufficient capital outlay to materially affect the existing financial condition of the utility involved, or will not result in increased charges to its customers.<sup>44</sup>

The Commission has interpreted 807 KAR 5:001, Section 15(3) as stating that no CPCN is required for extensions “that do not result in the wasteful duplication of utility plant, do not compete with the facilities of existing public utilities, and do not involve a sufficient capital outlay to materially affect the existing financial condition of the utility involved or to require an increase in utility rates.”<sup>45</sup> The Commission has almost always indicated that proposed construction that exceeds 10 percent or more of a utilities net plant in service is material and, therefore, requires a CPCN,<sup>46</sup> but has also found that smaller capital investments require a CPCN.<sup>47</sup>

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<sup>43</sup> Case No. 2000-00481, *Application of Northern Kentucky Water District (A) for Authority to Issue Parity Revenue Bonds in the Approximate Amount of \$16,545,000; and (B) A Certificate of Convenience and Necessity for the Construction of Water Main Facilities* (Ky. PSC Aug. 30, 2001), Order at 4.

<sup>44</sup> 807 KAR 5:001, Section 15(3) (emphasis added).

<sup>45</sup> Case No. 2000-00481, *Northern Kentucky Water District* (Ky. PSC Aug. 30, 2001), Order at 4.

<sup>46</sup> See, e.g., Case No. 2014-00277, *In the Matter of: Springcrest Sewer Co., Inc. Request for Deviation from 807 KAR 5:071, Section 7(4)*, (Ky. PSC Dec. 16, 2014) Order (finding that a remote monitoring system that exceeded 10% of a utilities net plant in service was material and, therefore, required a CPCN).

<sup>47</sup> See, e.g., Case No. 2018-00281, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates*, (Ky. PSC May 7, 2019) Order (discussing a 2% materiality threshold).

There is really no question, based on the records presented in the current matter, that Bluegrass Water's capital projects collectively are material to Bluegrass Water's existing financial condition and will result in increased charges to Bluegrass Water's customers, either now or in the future. Conversely, some individual "construction items" identified for specific systems likely would not materially affect Bluegrass Water's financial condition. Thus, the question regarding the application of the ordinary course of business exception is whether Bluegrass Water's proposed repairs, replacements, and improvements should be reviewed for materiality separately, collectively, or in some other combination.

Neither the statute nor the regulation explicitly state when various projects and subprojects should be considered a single extension for the purpose of determining whether construction falls into the stated exception. However, the Court in *Kentucky Utilities Co. v. Pub. Serv. Comm'n.*, 252 S.W.2d 885 (Ky. 1952) noted the absence of wasteful duplication is an element for determining whether to grant a CPCN and then defined wasteful duplication as "an excess of capacity over need" and "an excessive investment in relation to productivity or efficiency, and an unnecessary multiplicity of physical properties." The Court further noted that:

An inadequacy of service might be such as to require construction of an additional service facility to supplement an inadequate existing facility, yet the public interest would be better served by substituting one large facility, adequate to serve all the consumers, in place of the inadequate existing facility, rather than constructing a new small facility to supplement the existing small facility. A supplementary small facility might be constructed that would not create duplication from the standpoint of an excess of capacity, but would result in duplication from the standpoint of an excessive investment in relation to efficiency and a multiplicity of physical properties.

If KRS 278.020(1) were interpreted in a manner that allowed a utility to avoid the CPCN requirements by breaking out each discrete construction item or subproject as a separate extension, then the utility could, in part, avoid the analysis anticipated by the Court in *Kentucky Utilities Co.* and the legislature by measuring a single item necessary to repair, replace, or improve existing plant against the alternative instead of measuring all necessary construction on that plant against the alternative. Further, while significant overall capital investment in a short period may raise questions regarding whether a CPCN is necessary for certain projects, it would similarly be inconsistent with the statute and the Commission's past practice to review all of a utility's capital projects in a given period when determining whether the ordinary course of business exception applies.

Here, the Commission finds that all of the repairs and updates proposed to each sewage treatment facility should be reviewed collectively to determine the applicability of the ordinary course of business exception. Bluegrass Water is proposing significant construction on many of its treatment facilities nearly simultaneously such that the wasteful duplication analysis will require a collective review of the projects to determine whether they will result in wasteful duplication. Further, while Bluegrass Water made some updates to construction proposed for some systems, the construction items Bluegrass Water is proposing for each system were generally developed as part of a single plan for each system.<sup>48</sup> Similarly, when asked about the projects that support the additions in the base period and the forecasted period, Bluegrass Water identified all

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<sup>48</sup> See Response to Staff's Second Request, Item 27, 2 PSC 27 Engineering Memos Unredacted.pdf.

construction on each system as a single project.<sup>49</sup> Thus, at a minimum, the Commission finds that the proposed construction for each system should be analyzed collectively to determine whether a CPCN is required and, if so, whether it should be granted.

In reviewing Bluegrass Water's proposed construction, the Commission finds that a CPCN is necessary or should have been obtained for the construction, which includes repairs and upgrades, to the wastewater treatment facilities at Airview, Brocklyn, and Delaplain, as proposed in Mr. Freeman's testimony. Among other things, Bluegrass Water's estimated cost for the proposed upgrades to the treatment facilities at each of those systems, not including the engineering costs, exceeded the value of Bluegrass Water's net plant in service at the beginning of the base period, based on the schedules Bluegrass Water filed with its application, before Bluegrass Water began significant work on any of the projects. The estimated costs of the proposed repairs and upgrades at those systems similarly made up a significant portion of Bluegrass Water's projected net sewer plant in service at the end of the base period, which includes some of the same work at issue. The cost of those facilities also would represent a significant portion of Bluegrass Water's revenue in both the base and the forecasted periods. Thus, the Commission finds that the proposed construction at those wastewater treatment plants are not extensions in the ordinary course of business and, therefore, that a CPCN must or should have been obtained pursuant to KRS 278.020(1).

The Commission also finds that a CPCN should have been obtained for the construction, including repairs and upgrades, to the wastewater treatment facilities at

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<sup>49</sup> See Response to Staff's Second Request, Item 6, 2-PSC-06\_(sewer).xlsx (in which Bluegrass Water was asked about all projects included as CWIP or plant in service and it identified all work on each system collectively as a single project).

River Bluffs, which Bluegrass Water reported cost about \$439,705 to date, not including remote monitoring equipment, despite an initial estimate of about \$120,000. As with the repairs and upgrades proposed at the treatment facilities mentioned above, that capital expenditure is significant in relation to Bluegrass Water's plant in service and its revenue. Thus, the Commission finds that the proposed construction at that wastewater treatment plant is not an extension in the ordinary course of business and, therefore, that a CPCN should have been obtained pursuant to KRS 278.020(1).

Lastly, the Commission finds that a CPCN should have been obtained before Bluegrass Water implemented and began construction of electronic monitoring with its Mission monitoring facilities. The Commission observes that Bluegrass Water's decision to implement electronic monitoring of all of its facilities in Kentucky is akin to other utilities seeking to implement Advanced Metering Infrastructure or related smart grid technology system wide where none previously existed. The Commission has often found that such plans are not extensions in the ordinary course of business and, therefore, that a CPCN is required for the initial implementation.<sup>50</sup> Additionally, here, based Mr. Freeman's testimony, the total capital costs of the proposed Mission monitoring equipment was approximately \$298,000 and the systems require the payment of monthly operating

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<sup>50</sup> Case No. 2021-00428, *Consideration of the Implementation of Smart Grid and Smart Meter Technologies*, (Ky. PSC Apr. 13, 2016) Order ("the Commission finds it appropriate for jurisdictional electric utilities to obtain CPCNs for major AMR or AMI meter investments and distribution grid investments for DA, SCADA or volt/var resources"); see also Case No. 2020-00336, *Electronic Application of Meade County Rural Electric Cooperative Corporation for a Certificate of Public Convenience and Necessity to Continue with the Full Deployment Installation of its Automated Metering and Infrastructure Systems*, Order (Ky. PSC Apr. 19, 2021); Case No. 2016-00152, *Application of Duke Energy Kentucky, Inc. for (1) A Certificate of Public Convenience and Necessity Authorizing the Construction of an Advanced Metering Infrastructure; (2) Request for Accounting Treatment; and (3) All other Necessary Waivers, Approvals, and Relief*, (Ky. PSC May 25, 2017) Order.

costs.<sup>51</sup> Such costs will result in an increase in the rates of Bluegrass Water's customers and are significant in the aggregate when compared to Bluegrass Water's plant balances and revenue. Thus, the Commission finds that the proposal to install remote monitoring equipment across Bluegrass Water's systems in Kentucky is not an extension in the ordinary course of business and, therefore, that a CPCN should have been obtained pursuant to KRS 278.020(1).

#### Discussion of Whether to Grant a CPCN

To obtain a CPCN, a utility must demonstrate a need for such facilities and an absence of wasteful duplication.<sup>52</sup>

"Need" requires:

[A] showing of a substantial inadequacy of existing service, involving a consumer market sufficiently large to make it economically feasible for the new system or facility to be constructed or operated.

[T]he inadequacy must be due either to a substantial deficiency of service facilities, beyond what could be supplied by normal improvements in the ordinary course of business; or to indifference, poor management or disregard of the rights of consumers, persisting over such a period of time as to establish an inability or unwillingness to render adequate service.<sup>53</sup>

As noted above, "wasteful duplication" is defined as "an excess of capacity over need" and "an excessive investment in relation to productivity or efficiency, and an

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<sup>51</sup> Freeman Testimony.

<sup>52</sup> *Kentucky Utilities Co. v. Pub. Serv. Comm'n.*, 252 S.W.2d 885 (Ky. 1952).

<sup>53</sup> *Id.* at 890.

unnecessary multiplicity of physical properties.”<sup>54</sup> To demonstrate that a proposed facility does not result in wasteful duplication, we have held that the applicant must demonstrate that a thorough review of all reasonable alternatives has been performed.<sup>55</sup> The fundamental principle of reasonable least-cost alternative is embedded in such an analysis. Selection of a proposal that ultimately costs more than an alternative does not necessarily result in wasteful duplication.<sup>56</sup> All relevant factors must be balanced.<sup>57</sup>

### Airview

Bluegrass Water reported that the Airview wastewater treatment facility was in poor condition at the time of acquisition and showed clear signs the previous owner had failed to properly operate or reinvest in the plant and facilities.<sup>58</sup> 21 Design, Bluegrass Water’s third party engineering firm, inspected Airview’s facilities, identified a number of deficiencies at Airview that needed to be corrected, and recommended certain projects to correct those deficiencies.<sup>59</sup> Bluegrass Water then entered into an Agreed Order with the Energy and Environment Cabinet (EEC) that, among other things, required Bluegrass

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<sup>54</sup> *Id.*

<sup>55</sup> Case No. 2005-00142, *Joint Application of Louisville Gas and Electric Company and Kentucky Utilities Company for a Certificate of Public Convenience and Necessity for the Construction of Transmission Facilities in Jefferson, Bullitt, Meade, and Hardin Counties, Kentucky* (Ky. PSC Sept. 8, 2005).

<sup>56</sup> See *Kentucky Utilities Co. v. Pub. Serv. Comm’n*, 390 S.W.2d 168, 175 (Ky. 1965). See also Case No. 2005-00089, *Application of East Kentucky Power Cooperative, Inc. for a Certificate of Public Convenience and Necessity for the Construction of a 138 kV Electric Transmission Line in Rowan County, Kentucky* (Ky. PSC Aug. 19, 2005).

<sup>57</sup> Case No. 2005-00089, *East Kentucky Power Cooperative, Inc.* (Ky. PSC Aug. 19, 2005), final Order at 6.

<sup>58</sup> Cox Testimony at 7.

<sup>59</sup> See Response to Staff’s Second Request, Item 27, 2 PSC 27 Engineering Memos Unredacted.pdf at JA 00180-JA 00183.

Water to file a corrective action plan (CAP) describing how it would cure the deficiencies identified in 21 Design’s engineering report.

In its application, Bluegrass Water proposed the following repairs and upgrades to Airview’s wastewater treatment facilities.

<u>Construction Item</u>		<u>Estimated Cost</u>
Install flow equalization storage (20,000 gal)	\$	55,000
Influent Pumps from flow eq	\$	15,000
Chainlink fence replacement	\$	25,000
Sludge Holding tank renovation	\$	5,000
Clarifier Repairs	\$	205,000
Replace diffusers in aeration tankage	\$	30,000
Replace RAS lines from clarifier	\$	15,000
Replace blower	\$	25,000
Replace effluent pipe	\$	15,000
Remove contact chamber from creek	\$	5,000
Access road repair	\$	15,000

The proposed construction items are consistent with the needs identified by 21 Design in its engineering report, the recommendations made by 21 Design in its report, and the proposals 21 Design made to the EEC on behalf of Bluegrass Water in its CAP.<sup>60</sup> Further, while alternatives to each construction item were not specifically discussed, alternatives appear to have been reviewed where appropriate.<sup>61</sup> Moreover, the Commission understands that previous efforts by the previous owners to connect Airview to Elizabethtown’s system, facilitated by the EEC and the Commission, failed. Thus, the Commission finds that the projects identified above are both needed and will not result in

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<sup>60</sup> See Response to Staff’s Second Request, Item 3, 2-PSC-03-AOs.pdf, 2-PSC-03\_Correspondence.pdf, 2-PSC-03\_CAPs.pdf; Response to Staff’s Second Request, Item 27, 2 PSC 27 Engineering Memos Unredacted.pdf at JA 00180-JA 00183.

<sup>61</sup> See e.g., Response to Staff’s Second Request, Item 3, 2-PSC-03\_Correspondence.pdf, 2-PSC-03\_CAPs.pdf; Response to Staff’s Second Request, Item 27, 2 PSC 27 Engineering Memos Unredacted.pdf, JA 00180-JA 00183.

wasteful duplication<sup>62</sup> and, therefore, that a CPCN should be granted for those portions of the projects that are not complete.

However, Bluegrass Water indicated at the hearing and in response to post-hearing request for information that work on most of the construction items identified was completed, which means that Bluegrass Water violated KRS 278.020(1) by failing to obtain a CPCN before it began construction on those items. The Commission will not grant a CPCN for construction that has been completed,<sup>63</sup> and by failing to obtain a CPCN, a utility risks a finding by the Commission barring recovery of the investment. The Commission declines to do so here, given the urgent need for the construction and the absence of wasteful duplication. However, in the future, Bluegrass Water should be aware that the Commission may exercise its discretion to penalize or bar recovery of capital costs on plant for which a utility failed to obtain a CPCN as required.

### Brocklyn System

Bluegrass Water reported that the Brocklyn system was in poor condition at the time of acquisition and exhibited signs of past mismanagement, poor operation practices, and an overall lack of investment.<sup>64</sup> Among other things, Bluegrass Water indicated that:

All steel tanks and plant components were severely corroded,  
and many treatment components had not been properly

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<sup>62</sup> This is especially true given that the actual cost of some of the projects was significantly lower than the estimated cost. See Bluegrass Water's response to the Attorney General's Post-Hearing Request for Information (Response to Attorney General's Post Hearing Request), Item 1, AG\_post-hearing\_DR01 (indicating that the final cost of the Clarifier Repairs was only \$5,471.00 and that the final cost to Replace Blower was only \$7,230).

<sup>63</sup> See Case No. 2003-00495, *Application of Classic Construction, Inc. for Approval of Transfer of Ownership of Collbrook Sewage Treatment Plant in Franklin County, Kentucky from Aquasource Utility, Inc.*, (Ky. PSC May 10, 2004) Order (The Commission will not issue a CPCN for construction that has been completed prior to a request for a CPCN.).

<sup>64</sup> Cox Testimony at 14.

maintained. Yard piping consisted of PVC and flexible lines placed above ground, when proper installation of such facilities requires them to be buried. . . . Stormwater from an uphill neighborhood was routed into an open dirt channel running between the lagoon and an on-site package treatment plant, resulting in severe erosion that threatened the structural integrity of the lagoon further putting the surrounding community at risk.<sup>65</sup>

21 Design inspected Brocklyn's facilities, identified a number of deficiencies at Brocklyn's wastewater treatment plant, and recommended certain repairs and upgrades to correct those deficiencies. Bluegrass Water then entered into an Agreed Order with the EEC that, among other things, required Bluegrass Water to file a CAP describing how it would cure the deficiencies identified in 21 Design's engineering report.

At Brocklyn, Bluegrass Water indicated that it closed the lagoon of the current treatment facility (though in its CAP and updates to EEC it referred to it as a clean out of the lagoon), made repairs to the sludge judge lagoon cell, and cleaned up sludge from the creek surrounding Brocklyn's sewage treatment plant.<sup>66</sup> Bluegrass Water had also initially proposed a number of repairs to its existing plant.<sup>67</sup> However, in a July 29, 2020 revision to its Brocklyn CAP, Bluegrass Water reported to the EEC that in the process of making repairs to the system that it determined that the tankage of the Brocklyn extended aeration plant is severely deteriorated such that the plant at Brocklyn would need to be

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<sup>65</sup> *Id.*

<sup>66</sup> Response to Attorney General's Post Hearing Request, Item 1, AG\_post-hearing\_DR01; see also Response to Staff's Second Request, Item 3, 2-PSC-03\_Correspondence.pdf (containing updates discussing Bluegrass Water's actions to comply Brocklyn's CAP).

<sup>67</sup> Response to Staff's Second Request, Item 3, 2-PSC-03\_CAPs.pdf (containing Bluegrass Water's initial CAP for Brocklyn).

replaced.<sup>68</sup> Bluegrass Water is now proposing to replace the wastewater treatment facility at Brocklyn in lieu of other proposed repairs<sup>69</sup> and estimated the cost of the plant would be \$650,000.<sup>70</sup>

The evidence indicates that there is a need to take action at Brocklyn to repair a significant issue with the existing plant, and Bluegrass Water did explore some alternatives to building a new package treatment plant in that it was initially attempting to simply repair the system.<sup>71</sup> However, while Bluegrass Water indicated its belief that connecting to the city of Richmond's sewer system would be more costly, Bluegrass Water acknowledged at the hearing that it had not fully weighed the feasibility or the cost of attaching the Brocklyn's collection to the city of Richmond's facilities.<sup>72</sup> Bluegrass Water indicated that it was currently in the process of completing that analysis, which EEC had requested from Bluegrass Water as part of the permitting process for the new plant proposed at Brocklyn.<sup>73</sup> The Commission finds that Bluegrass Water has not yet explored all reasonable alternatives with respect to the proposed new sewage treatment plant at Brocklyn and, therefore, that the required CPCN should be denied without

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<sup>68</sup> Response to Staff's Second Request, Item 3, 2-PSC-03\_Correspondence.pdf (containing the July 29, 2020 letter).

<sup>69</sup> *Id.*

<sup>70</sup> Response to Staff's Second Request, Item 3, 2PSC12-03\_RateBase(Brocklyn).xlsx at Tab CWIP – BY B4.

<sup>71</sup> Response to Staff's Second Request, Item 3, 2-PSC-03\_Correspondence.pdf (containing the July 29, 2020 letter); Response to Staff's Second Request, Item 3, 2-PSC-03\_CAPs.pdf (containing Bluegrass Water's initial CAP for Brocklyn in which it was initially proposing to repair the treatment plant); Response to Staff's Second Request, Item 3, 2-PSC-03\_Correspondence.pdf (containing the July 29, 2020 letter in which Bluegrass indicated that it would need to repair the plant).

<sup>72</sup> May 20, 2021 H.V.T at 11:20:05-11:22:18.

<sup>73</sup> May 20, 2021 H.V.T at 11:20:05-11:22:50.

prejudice. Bluegrass Water should refile the request when it has explored all reasonable alternatives.

### Delaplain System

Bluegrass Water did not own the Delaplain system at the time that the application in this matter was filed, but Bluegrass Water reported that it had identified a number of problems with the system as part of its preliminary due diligence to purchase the system that it contended must be addressed immediately after closing and within the period covered by the forecasted test year.<sup>74</sup> Bluegrass Water indicated that the primary issue facing the facility is that “flows massively exceed its design capacity,” which Bluegrass Water stated indicates that the facility is undersized and needs to be expanded to treat the high volume waste loading the facility receives rather than just attempting to reduce infiltration and inflow of the system.<sup>75</sup> Bluegrass Water proposed to convert and expand the waste water treatment plant at an estimated cost of over \$800,000 to address that capacity shortfall as well as other issues identified with the Delaplain system.<sup>76</sup>

Bluegrass Water indicated that discussions with the City of Georgetown regarding Georgetown’s ability to take waste from Delaplain, as opposed to increasing capacity at the treatment plant, are ongoing.<sup>77</sup> Bluegrass Water indicated that there were some preliminary discussions with Georgetown before Bluegrass Water purchased the Delaplain system and that Delaplain’s engineering firm reached out for more formal

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<sup>74</sup> Freeman Testimony at 44.

<sup>75</sup> Freeman Testimony at 45; see also Response to Staff’s Second Request, Item 27, 2 PSC 27 Engineering Memos Unredacted.pdf; May 19, 2021 H.V.T at 9:39:50.

<sup>76</sup> Freeman Testimony at 44-46;

<sup>77</sup> See May 20, 2021 H.V.T at 11:15:15.

discussions in about March of 2021.<sup>78</sup> Bluegrass Water indicated that the discussions are ongoing and that Georgetown is preparing a proposal with the details of what Delaplain would have to do to connect to Georgetown's systems.<sup>79</sup> Bluegrass Water did not have a specific timetable regarding when it would receive a proposal from the city but at the time of the hearing indicated that they expected it within a month.<sup>80</sup>

While the Commission understands that Bluegrass Water anticipates that the cost of connecting to Georgetown's system will be more than simply expanding its own plant, Bluegrass Water is still waiting on Georgetown's proposal, and the analysis of wasteful duplication and the reasonable least cost alternative is not simply about the capital cost of the project. In this instance, the Commission finds that Bluegrass Water cannot establish the absence of wasteful duplication with respect to the expansion at the Delaplain system until it has received and evaluated the proposal from Georgetown. Thus, the Commission finds that the CPCN for the proposed treatment plant conversion and expansion at Delaplain should be denied without prejudice.

#### River Bluffs System

Bluegrass Water reported that River Bluffs has a long history of non-compliance with environmental regulations and that maintenance at the facility had been poor.<sup>81</sup>

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<sup>78</sup> May 20, 2021 H.V.T at 11:17:28.

<sup>79</sup> See May 20, 2021 H.V.T at 11:15:15.

<sup>80</sup> See May 20, 2021 H.V.T at 11:15:15.

<sup>81</sup> Cox Testimony at 56–58.

Bluegrass Water indicated in testimony filed with the application in this matter that the following repairs and improvements would be necessary:<sup>82</sup>

<u>Construction Item</u>		<u>Estimated Cost</u>
Address Inflow and Infiltration	\$	25,000.00
Mission Monitoring	\$	18,000.00
Lift station cleanup	\$	33,000.00
Control Panel Replacement	\$	10,000.00
Replace influent/exposed PVC pipe	\$	10,000.00
Treatment facility cleanup and repair	\$	20,000.00
Replace diffusers and blowers	\$	32,500.00
Replace air header	\$	5,000.00
Replace sludge returns	\$	10,000.00

Bluegrass Water noted that it had only recently closed on its acquisition of the River Bluffs system and that many of the planned improvements had not been completed, but Bluegrass Water noted that “items such as basic site cleanup and the proper installation of the influent line have been completed” and that “[r]epairs and patching of corroded steel tankage are underway and continue.”<sup>83</sup>

Bluegrass Water presented an engineering report that generally supported the need for the proposed construction items. The evidence for the construction as proposed supported the need and the absence of wasteful duplication.<sup>84</sup> Thus, while the Commission could not grant a CPCN for work that had already been completed, it could allow Bluegrass Water to recover the cost of the projects through rates as it did for the projects Bluegrass Water completed at Airview without obtaining a CPCN.

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<sup>82</sup> Freeman Testimony at 33–34.

<sup>83</sup> Freeman Testimony at 33.

<sup>84</sup> Response to Staff’s Second Request, Item 27, 2 PSC 27 Engineering Memos Unredacted.pdf (containing River Bluffs Report); Response to Staff’s Second Request, Item 3, 2-PSC-03\_Correspondence.pdf, 2-PSC-03\_CAPs.pdf.

However, in response to post hearing requests for information from the Attorney General, Bluegrass Water indicated that several of the construction items proposed were significantly over budget. Specifically, Bluegrass Water indicated that the treatment facility cleanup and repair cost \$231,579 to complete despite an estimated cost of \$20,000; the replacement of diffusers and blowers cost \$96,559 to complete despite an estimated cost of \$32,500; and the replacement of the air header cost \$35,000 to complete despite an estimated budget of \$5,000.

While projects may occasionally go over budget, the extent by which the construction items identified above went over budget indicate that the work completed does not represent the same work initially contemplated. Further, the CAP for River Bluffs, which Bluegrass Water used to justify the construction, and correspondence between Bluegrass Water and the EEC do not indicate a significant change in the scope of the work.<sup>85</sup> Bluegrass Water has also indicated it is contemplating a new plant at River Bluffs,<sup>86</sup> such that any repairs made at this time may not provide long term benefits to customers. Thus, based on the current record, the Commission is not able to find that the repairs and upgrades that resulted in the construction items being significantly over budget are needed and will not result in wasteful duplication.

Based on the finding above, the Commission will adjust Bluegrass Water's rate base below based on the extent those construction items went over budget. However,

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<sup>85</sup> See Response to Staff's Second Request, Item 3, 2-PSC-03\_Correspondence.pdf, 2-PSC-03\_CAPs.pdf.

<sup>86</sup> See Response to Staff's Second Request, Item 3, 2-PSC-03\_CAPs.pdf (where Bluegrass Water stated in a July 30, 2020 CAP for River Bluffs that "[f]ollowing these initial improvements, a period of observation and evaluation will be conducted to determine if a process change is needed at the facility to consistently meet limits that the facility has struggled with in the past"); see also Response to Staff's Second Request, Item 27, 2 PSC 27 Engineering Memos Unredacted.pdf (containing River Bluffs Report).

for the reasons Bluegrass Water is being allowed to recover its investment in Airview, the Commission may allow Bluegrass Water to recover the amounts excluded from River Bluffs here as part of a subsequent rate case if Bluegrass Water later establishes, as part of that case, that the additional costs were for capital spending at River Bluffs that was needed and did not result in wasteful duplication.

#### Implementation of Remote Monitoring

Bluegrass Water installed or proposed to install remote monitoring equipment at most of its systems. In response to the Attorney General's First Request for Information, Item 6, Bluegrass Water explained that remote monitoring is necessary, because it "increases the effectiveness of operations at basic sewage plants and collection systems and drives down costs related to improvements and environmental compliance that would otherwise be passed through to customers." However, while remote monitoring does appear to provide more continuous access to data than having an operator inspect the systems daily, as required by 807 KAR 5:071, Section 7(4), the remote monitoring systems, at least in part, serve the same purpose as that requirement by ensuring that a utility is constantly monitoring the performance of equipment to prevent failures and ensure adequate service. Bluegrass Water indicated that operator costs in Kentucky were higher than those for Bluegrass Water affiliates in other states precisely because it required its operators to comply with 807 KAR 5:071, Section 7(4), which is not required in other states, such that the benefits of remote monitoring in Kentucky are at least reduced. Finally, Bluegrass Water acknowledged that it had not performed any cost

benefit analysis of the installation of the monitoring equipment in Kentucky.<sup>87</sup> Because, the costs of remote monitoring are not immaterial,<sup>88</sup> the Commission finds that Bluegrass Water failed to establish the absence of wasteful duplication.

#### Additional Construction

Pursuant to 807 KAR 5:001, Section 19(1), the Commission may, in its discretion, issue a declaratory order with respect to . . . the applicability to a person, property, or state of facts of an order or administrative regulation of the commission or provision of KRS Chapter 278.” While the Commission may choose to exercise its discretion and address an application for a declaratory order, it may similarly choose not to address an application for a declaratory order. This regulation is primarily intended as a mechanism to provide utilities guidance in situations involving new or novel issues that might be difficult to resolve through construction of the Commission’s orders or regulations, or KRS Chapter 278.

A number of utilities have been abusing 807 KAR 5:001, Section 19 recently by failing to request a CPCN where one is clearly required and instead requesting an order from the Commission that a CPCN is not required or by requesting a declaratory order that all proposed spending in a given period does not require a CPCN and requesting a CPCN in the alternative. The declaratory order regulation is not intended to resolve such issues. Rather, an application for a CPCN should be filed where a CPCN is obviously required, an application for a declaratory order should only be filed where there is a

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<sup>87</sup> May 19, 2021 H.V.T at 09:45:00.

<sup>88</sup> The capital costs ranged from about \$7,500 to \$50,000 per system; Bluegrass Grass indicated that the equipment would last 5 to 10 years; and there is a monthly subscription fee per system.

legitimate question regarding whether a CPCN is required, and utilities should not routinely request that the Commission review all spending in a given period to determine what does and does not require a CPCN.

Here, as noted above, Bluegrass Water claimed in its application that no CPCN was required despite proposing approximately \$7.5 million in capital spending, including projects to replace or significantly upgrade existing wastewater treatment plants. Bluegrass Water's claims that no CPCN is required for the new plant at Brocklyn or the expansion at Delaplain, which it backed away from in testimony, are absurd on their face. Further, it should have been clear, between precedent and a plain reading of the law, that the additional construction discussed above required a CPCN. Thus, Bluegrass Water should not have requested a declaratory order or in the alternative requested a CPCN, but rather, should have specifically requested a CPCN for the projects that required it.

The Commission could have simply exercised its discretion and declined to address the application for the declaratory order and, in turn, the application for a CPCN. The Commission did not do so here for the projects discussed above, because Bluegrass Water is not the only utility that has recently engaged in this practice. However, while the construction items not specifically addressed above appear to be necessary and do not appear to result in wasteful duplication, the Commission does decline to make a specific finding that each additional construction item not discussed above is an extension in the ordinary course of business. Further, in the future, if Bluegrass Water or another utility files an application for a declaratory order finding that a CPCN is not required where one is clearly required or that all proposed spending does not require a CPCN, the Commission may decline to address any part of the application and, in turn, refuse to

grant any alternative application for a CPCN even where a CPCN is clearly necessary, which may be considered in denying a utility recovery the cost of such plant in the future.

## RATES

### Legal Standard

Bluegrass Water filed its application for a rate adjustment pursuant to KRS 278.180 and KRS 278.190. The Commission's standard of review of a utility's request for a rate increase is well established. In accordance with statutory and case law, Bluegrass Water is allowed to charge its customers "only 'fair, just, and reasonable rates.'"<sup>89</sup> Further, Bluegrass Water bears the burden of proof to show that the proposed rate increase is just and reasonable, under KRS 278.190(3).

### Test Period

Bluegrass Water proposed the 12 months ending April 30, 2022, as its forecasted test period to determine the reasonableness of its proposed rates.<sup>90</sup> The Attorney General and Joint Intervenors did object to the proposed test period for the reasons discussed above and requested that a historical test period be used for some of the systems, but as discussed above, the Commission did not find that their objections justified rejecting the forecasted test period. For the reasons discussed above and based on the record in this matter, the Commission finds Bluegrass Water's forecasted test period to be reasonable and consistent with the provisions of KRS 278.192 and 807 KAR 5:001, Section 16(6), (7), and (8). Therefore, the Commission will accept the forecasted test year proposed by Bluegrass Water for use in this proceeding.

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<sup>89</sup> KRS 278.030; and *Pub. Serv. Comm'n v. Com. ex rel. Conway*, 324 S.W.3d 373, 377 (Ky. 2010).

<sup>90</sup> Application at 4.

## VALUATION

### Sewer Rate Base

Bluegrass Water proposed a forecasted net investment rate base for its sewer division of \$6,907,546 based on a 13-month average for that period.<sup>91</sup> In its base period update, Bluegrass Water increased its proposed sewer rate base to \$7,689,482.<sup>92</sup> As discussed in more detail below, the Commission does not believe Bluegrass Water's rate base numbers are credible. Rather, the Commission finds that Bluegrass Water's net investment sewer rate base in the forecasted test period, excluding the 00297 systems, is \$2,601,721, as shown below.

### Utility Plant In Service (UPIS)

Bluegrass Water reported a base year sewer UPIS ending balance of \$4,305,222.<sup>93</sup> According to Bluegrass Water, its base year UPIS balance reflected the actual amounts recorded on its books as of August 31, 2020, and the forecasted UPIS additions for the four-month period ending December 31, 2020.<sup>94</sup> Bluegrass Water explained that its 13-month average UPIS of \$8,438,874 in the forecasted period was calculated by adding forecasted acquisitions and plant additions and subtracting forecasted retirements through April 2022.<sup>95</sup>

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<sup>91</sup> Responses to Staff's First Request, Item 1, BGUOC2020RateCase-RateBase\_(Sewer).xlsx, Tab FY Rate Base - Sewer B1.

<sup>92</sup> Base Period Update (filed Mar. 19, 2021), Excel Workbook: BYupdate-RateBase\_(Sewer).xlsx, Tab FY Rate Base - Sewer B1.

<sup>93</sup> Response to Staff's First Request, Item 1, BGUOC2020RateCase-RateBase\_(Sewer).xlsx, Tab UPIS - BY B2.

<sup>94</sup> Application, Exhibit 8, Thies Direct Testimony at 13.

<sup>95</sup> *Id.*

Joint Intervenors noted that Bluegrass Water had committed to account for its plant retirements through the forecasted test year.<sup>96</sup> Upon review of Bluegrass Water's filing of its base year updates, Joint Intervenors argue that Bluegrass Water had not recorded UPIS retirements in either the base period or the forecasted test year.<sup>97</sup> Joint Intervenors argue that Bluegrass Water's lack of attention to detail is not credible and is unacceptable for a regulated utility.<sup>98</sup>

Joint Intervenors also note that Bluegrass Water asserted in its application that it would invest approximately \$7.56 million (\$6.4 million in its wastewater division and \$1.16 million in its water division) and that it would complete that investment prior to the end of the forecasted test year on April 30, 2022. However, Joint Intervenors point out that Bluegrass Water identified less than \$2 million that has actually been spent on construction across Bluegrass Water's entire system.<sup>99</sup>

The Attorney General similarly notes that Bluegrass Water's witness, Brent Thies, under questioning from Vice-Chairman Chandler at the hearing, testified that Bluegrass Water failed to reflect any plant retirements in developing its Forecasted Test-Year UPIS.<sup>100</sup> The Attorney General claims that Bluegrass Water failed to determine if plant

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<sup>96</sup> Joint Intervenors Brief at 10.

<sup>97</sup> *Id.* at 10–11.

<sup>98</sup> *Id.* at 11.

<sup>99</sup> *Id.*

<sup>100</sup> Brief of the Attorney General at 4–5.

retirements were appropriate and that such an incomplete analysis would inflate Bluegrass Water's revenue requirement to the detriment of ratepayers.<sup>101</sup>

According to Bluegrass Water, both intervenors assert that there must have been retirements from UPIS and that UPIS retirements must be included as net subtractions in the base or forecasted test year schedules.<sup>102</sup> Bluegrass Water argues that neither the Attorney General nor Joint Intervenors acknowledge or address the explanation that was given in the hearing by Brent Thies that the lack of plant retirements in the designated columns was not material due to offsetting accumulated depreciation.<sup>103</sup> Joint Intervenors argue that Bluegrass Water lacks the accounting records necessary to demonstrate that the claim presented by Mr. Thies at the hearing is accurate.<sup>104</sup>

With respect to Joint Intervenors assertion that Bluegrass Water has spent under \$2 million on construction that could be reflected as additions across the entire system, Bluegrass Water argues that the data request and response cited in support of that statement relate to the planned projects itemized in Mr. Freeman's direct testimony that were partially or fully complete at the time of his hearing testimony, not expenditures for projects on the entire Bluegrass Water system since September 2019.

The Commission agrees with the Joint Intervenors and the Attorney General regarding the lack of supporting evidence for Bluegrass Water's UPIS. First, schedules and spreadsheets provided by Bluegrass Water include conflicting information. As noted

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<sup>101</sup> *Id.*

<sup>102</sup> Bluegrass Water's Brief at 11.

<sup>103</sup> *Id.* at 11–12.

<sup>104</sup> Joint Intervenors' Brief at 9.

above, Bluegrass Water calculated the 13-month average of its sewer UPIS in the application and attached schedules as \$8,438,874.<sup>105</sup> Then, in responding to a request from Commission Staff, Bluegrass Water provided separate Excel workbooks with the 13-month average rate base for each separate system that it had acquired or was seeking to acquire prior to the beginning of the forecasted period.<sup>106</sup> Upon the Commission’s review of the individual system rate bases, it was noted that total UPIS for the 19 systems did not equal the amount reported by Bluegrass Water in its application as shown in the table below.

	UPIS Staff 2nd Request Item 12
Woodland Acres	\$ 80,163
Timberland	125,127
Springcrest	49,200
River Bluff	596,176
Randview	139,973
Persimmon Ridge	504,609
Marshell Ridge	60,597
LH Treatment	679,447
Columbia	327,264
Kingswood	367,133
Haven	60,728
Grest Oaks	233,347
Golden Acres	204,283
Fox Run	348,728
Delaplain	2,252,079
Carriage Park	60,408
Brocklyn	659,362
Arcadia Pines	46,563
Airview	402,073
UPIS Totals	7,197,260
Application 13-Month Average UPIS and CWIP	(8,438,874)
Difference	\$ (1,241,614)

<sup>105</sup> Application, Exhibit 8, Thies Testimony at 13; Response to Staff’s First Request, Item 1, Excel Workbook: BGUOC2020RateCase-RateBase\_(Sewer).xlsx, Tab UPIS - FY B2.

<sup>106</sup> Responses to Staff’s Second Request, Item 12.

This discrepancy raises questions regarding what Bluegrass Water included in UPIS. When Bluegrass Water was asked to provide the system specific information as originally requested in a post hearing request for information, Bluegrass Water stated that “[d]ue to the process used to update rate base numbers at the end of the base period, the data source necessary to produce system level rate base specific numbers is no longer available.”<sup>107</sup> Nevertheless, Bluegrass Water attempted to explain the discrepancy by stating:

A data source was inadvertently omitted from the Utility Plant in Service totals for the system. This data source was CWIP balances that were on the books of Bluegrass Water as of 12/31/2020 but the assets were not yet placed into service.

Bluegrass Water’s explanation does not resolve questions regarding what Bluegrass Water included in UPIS, including how CWIP was accounted for and whether the forecasted UPIS has been reported net of Accumulated Depreciation, Plant Acquisition Adjustments, or CIAC. Further, Bluegrass Water’s explanation does not provide any way to assess the UPIS Bluegrass Water included in the forecasted period for each system, as filed with its application, in order to check the proposed UPIS and CWIP changes against Bluegrass Water’s projected projects.

More problematic, the undisputed evidence indicates Bluegrass Water did not include any retirements in the base period, the forecasted test year, or the period between the base and forecasted periods despite providing sworn testimony with its application

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<sup>107</sup> Responses to Staff’s Hearing Data Request, Item 1.a.

that it had done so.<sup>108</sup> As Bluegrass Water acknowledged, changes to UPIS are calculated in a given period by taking the starting balance of the UPIS, adding the additions, and then subtracting the retirements such that the net change is reflected at the end of the period.<sup>109</sup> Moreover, it is clearly understood and expected that if a utility is projecting that it will incur significant capital costs to repair, replace, and upgrade existing plant that it will have retirements. When asked to explain why Bluegrass Water did not account for retirements, Bluegrass Water's witness stated that he did not really have an explanation except that some, or most, existing assets were fully depreciated such that Bluegrass Water recognized the "negligible" impact the retirements would have on plant in service and, therefore, did not focus on projecting retirements.<sup>110</sup> However, by calculating UPIS in that manner, Bluegrass Water focused solely on the positive side of equation that will increase UPIS, while ignoring any change to the negative side of the equation that might decrease UPIS. In short, Bluegrass Water essentially testified at the hearing that it focused on projecting amounts that increased its projected UPIS and, therefore its revenue requirement, while ignoring the component that would decrease the UPIS.

Bluegrass Water claimed at the hearing and in its brief that its failure to account for retirements had minimal or no effect on rates, because the existing plant of the systems it purchased had largely been depreciated and, therefore, that property

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<sup>108</sup> May 19, 2021 H.V.T. at 15:45:33, 16:39:00; 16:44:00; see *also* Response to Staff's Second Request, Item 5 and 7, 2-PSC-05b.xlsx, 2-PSC-07b.xlsx (showing no retirements during any of the relevant periods).

<sup>109</sup> See May 19, 2021 H.V.T. at 16:37:50-16:40:24.

<sup>110</sup> See May 19, 2021 H.V.T at 16:39:25.

Bluegrass Water should have retired was being offset by accumulated depreciation, which would be eliminated when the plant was retired, such that its failure to include retirements had no net effect on rates. However, Bluegrass Water's explanation falls apart for two reasons. First, while it appears that some of the systems Bluegrass Water purchased were fully depreciated,<sup>111</sup> all of the systems were not fully depreciated such that some assets with a net plant balance likely would be retired given the scope of the work Bluegrass Water was proposing. Second, Bluegrass Water calculated depreciation expense in the base and forecasted periods by applying depreciation rates to its UPIS<sup>112</sup> and, therefore, Bluegrass Water's model would include depreciation expense on UPIS that should have been retired even if that UPIS is fully offset in rate base by corresponding accumulated depreciation.<sup>113</sup> Thus, Bluegrass Water's failure to project retirements of UPIS during any period from at least January 1, 2020, through April 30, 2022, when it was engaging in significant capital spending did materially impact rates.

Bluegrass Water's failure to account for retirements in projecting UPIS and other discrepancies in its rate base schedules place the Commission in a difficult position in attempting to set a rate base to which a rate of return and depreciation rates should apply

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<sup>111</sup> There is no evidence in the record regarding the extent to which the assets of the systems were depreciated when Bluegrass Water purchased them. Commission Staff requested in a post hearing request for information that Bluegrass Water provide the original cost of the acquired assets of each system along with the associated accumulated depreciation by NARUC account. Bluegrass Water provided the plant balances projected for the end of the forecasted period and the projected accumulated depreciation for the end of the forecasted period. See Response to Staff's Post-hearing Request, Item 2. However, in response to Joint Intervenors' post hearing request for information, Bluegrass Water did provide the rate base of each system at the time of acquisition, which indicated that that most of the systems had little to no rate base. See Response to Joint Intervenors' Post-Hearing Request, Item 12, INTphDR12a.xlsx.

<sup>112</sup> See Response to Staff's First Request, Item 1, BGUOC2020RateCase-RateBase\_(Sewer).xlsx, Tab Dep - FY B3.1 (showing that depreciation expense for a particular account is calculated by multiplying the utility plant in service balance by the depreciation rate).

<sup>113</sup> See May 20, 2021 at 09:22:23–09:25:30.

when setting rates. As Bluegrass Water acknowledged, the original cost of the assets for many of the systems Bluegrass Water purchased in this matter were fully depreciated when Bluegrass Water purchased them. However, assuming depreciation was properly tracked by the previous owners, limited portions of some systems were not fully depreciated at the time the systems were transferred to Bluegrass Water.<sup>114</sup> The problem is that the evidence regarding UPIS and accumulated depreciation for each sewer system at the time of transfer is limited, and there is no specific evidence in the record regarding the portions of the UPIS for each sewer system at the time of transfer that should have been retired as Bluegrass Water made projected repairs, replacements, and improvements, because Bluegrass Water did not project any retirements.

Bluegrass Water did provide some consideration to the previous owners of the systems at issue for the systems' assets. However, Bluegrass Water did not propose or present evidence in support of a system acquisition adjustment in this matter to recover those acquisition costs to the extent they exceeded the net value book value of the systems.<sup>115</sup> In fact, although related cases indicate that the acquisition costs for the systems at issue in this matter were limited, there was limited to no evidence regarding the consideration provided to purchase the assets of the systems at issue.<sup>116</sup>

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<sup>114</sup> Again, the system specific schedules did not match the system wide schedules filed with the application. Bluegrass Water did not response to Commission Staff's post hearing request for information asking for the original cost of the acquired assets and associated accumulated depreciation by NARUC account. See Response to Staff's Post-Hearing Request, Item 2.

<sup>115</sup> May 20, 2021 H.V.T. at 09:15:30.

<sup>116</sup> The only evidence as to purchase prices identified by the Commission was anecdotal. For instance, at the hearing, when Bluegrass Water was discussing why its failure to account for retirements had little effect, it displayed and discussed a journal entry for Brocklyn indicating that the total payments at closing were \$14,350.90. May 20, 2021 H.V.T. at 09:11:40, Exhibit 2. Similarly, in response to Commission Staff's Third Request, Item 3, Bluegrass Water provided the sales contract for the LH Treatment Company, LLC in support of an O&M expense and that contract contained the sale price of \$230,000.

For the reasons discussed above and being otherwise sufficiently advised, the Commission finds that Bluegrass Water failed to establish the existing UPIS and accumulated depreciation for the systems at issue in this matter at the time of acquisition and the extent to which those assets should have been retired during the base period, the forecast period, and the period between the base and the forecasted period. The Commission observes that intervenors suggest that the Commission should dismiss this matter, in part, due that failure and that is a potential solution. However, the Commission finds that such a solution would not be in the long term interest of Bluegrass Water or its customers given Bluegrass Water's financial position and the need to attract additional capital to provide service and necessary upgrades to systems that have seen little investment in many years. Instead, the Commission will remove any UPIS and accumulated depreciation associated with the systems at the time of the acquisitions in this matter. To accomplish this, the Commission will calculate UPIS by simply adding the original cost of the projects Bluegrass Water indicated it had completed or would complete in 2019, 2020, the forecasted period, and the period between the base period and the forecast period and will calculate accumulated depreciation by eliminating accumulated depreciation prior to the forecasted period, which would nearly all be attributed to depreciation that occurred prior to Bluegrass Water's acquisitions of the various systems.

Specifically, with respect to the UPIS, the Commission will use the spreadsheet provided by Bluegrass Water in response to Commission Staff's Second Request, Item 6. In response to that request, Bluegrass Water provided a spreadsheet, at the end of February 2021, with the total actual cost of each project, if completed, or the total expected cost of each project that Bluegrass Water contends supports that projected

additions or CWIP in the schedules filed with the application for the base period, the forecasted period, and the months between the base and the forecasted periods, as well as the date on which work on each project began or is expected to begin and the date on which each project was placed in service or is expected to be placed in service.<sup>117</sup>

The Commission submits that the information provided in response to Staff's Second Request, Item 6, should reflect, by Bluegrass Water's own admission, all projects that support additions to UPIS in the period from January 1, 2020, about four months after Bluegrass Water began operating any of the systems, through the end of the forecasted period. The Commission notes that spreadsheet also justifies the spending by referring to both Mr. Cox and Mr. Freeman's testimony, which supports the finding that it includes actual or projected spending discussed by both witnesses. Bluegrass Water also provided the actual and projected dates on which its proposed spending would begin and the actual or projected in service dates such that it is possible to determine when projects should be moved from CWIP to UPIS and, using Bluegrass Water's straight-line method for projecting CWIP spending,<sup>118</sup> when projected spending will occur during the forecasted period in order to calculate the 13-month average of CWIP and UPIS.

The issue with the using the information provided in response to Staff's Second Request, Item 6 is that Bluegrass Water apparently failed to include the projects for Persimmon Ridge and arguably there could have been spending on projects that occurred in 2019 that would not be include with that information. To address the issue of the

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<sup>117</sup> Response to Staff's Second Request, Item 6, 2-PSC-06.xlsx.

<sup>118</sup> See May 20, 2021 H.V.T. at 12:01:54–12:02:38 (in which Mr. Duncan states that CWIP during forecasted period was projected based on a straight line of the remaining projected spending and the project end date).

Persimmon Ridge projects, the Commission will use the construction information provided in Mr. Freeman's testimony for Persimmon Ridge, which was largely complete as of the date of the hearings, and a final in service date for the Persimmon Ridge construction of September 2021 based on the final in service dates of the other systems included therein. To address construction in 2019, the Commission will only include construction for which there is evidence it was actually completed in 2019 in Bluegrass Water's response to the Attorney Generals post-hearing request for information.<sup>119</sup>

Using the method discussed above, and removing any construction for the 00297 systems, the 13-month average UPIS balance calculated by the Commission as shown in Appendix A is \$1,719,678. That UPIS balance is \$6,719,196 below the UPIS balances projected by Bluegrass Water in the forecasted period. However, the Commission notes that it is making this adjustment, in part, because Bluegrass Water failed to meet its burden with respect to amounts removed, including UPIS and accumulated depreciation at the time of transfer and the extent to which those amounts should have been retired. This Order should not be construed as preventing Bluegrass Water from seeking to include those amounts, should it choose to do so, in rate base in a future rate proceeding with proper supports.

Construction Work In Progress (CWIP). Bluegrass Water defines CWIP as the value of utility plant that is under construction but has not yet been placed into service.<sup>120</sup> Bluegrass Water's forecasted CWIP of \$877,758 is based on a thirteen-month average

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<sup>119</sup> Response to Attorney General's Post-Hearing Request, Item 1, AG\_post-hearing\_DR01.xlsx, Tab Construction Invoices (showing \$298,830 in spending in 2019).

<sup>120</sup> Application, Exhibit 8, Thies Testimony at 13.

of the forecasted balances from April 1, 2021, through April 30, 2022.<sup>121</sup> Using the construction completed in the forecasted test-year and excluding CWIP for the 00297 systems, as discussed above for UPIS, the Commission calculated a 13-month average CWIP in the forecasted period of \$761,724, which is \$116,034 below Bluegrass Water's forecasted CWIP. The Commission's calculation of its 13-month average CWIP is included in Appendix A.

Brocklyn Plant Replacement. As noted above, the Commission denied the CPCN for the Brocklyn plant replacement at this time. Bluegrass Water projected the cost of the plant replacement would be approximately \$650,000.<sup>122</sup> The Commission removed that project from CWIP and UPIS by removing \$650,000 from the total projected budget for Brocklyn shown in response to Staff's Second Request, Item 6. The Commission then included the remainder of the projected budget in UPIS as shown in Appendix A.

River Bluffs Plant Project. As noted above, the Commission denied a CPCN for three projects at River Bluffs with an original projected cost of \$57,500.00 to the extent that they were over budget by \$305,638 and found that Bluegrass Water failed to establish the need for that expanded project or the absence of wasteful duplication. Based on total costs reflected for River Bluffs in response to Staff's Second Request, Item 6 as compared to the original budget in Mr. Freeman's testimony, the Commission finds that those additional costs were included in the response and, therefore, must be adjusted here based on the findings discussed above. Thus, as shown in Appendix A, the Commission

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<sup>121</sup> *Id.*

<sup>122</sup> Response to Staff's Second Request, Item 3, 2PSC12-03\_RateBase(Brocklyn).xlsx at Tab CWIP-BY B4.

removed that amount from UPIS and CWIP for the River Bluffs system when calculating the 13-month average discussed above.

Canceled Construction Items. Bluegrass Water's witness testified at the hearing that in consultation with their third party engineering firm that Bluegrass Water had decided to eliminate several projects at Lake Columbia just prior to the hearing. Specifically, he stated that they had decided to eliminate the flow equalization and pumping system item with a projected cost of \$40,000, the install aeration in flow equalization and sludge holding item with a projected cost of \$15,000, and the collection system repair for I&I item with a projected cost of \$30,000. Since Bluegrass Water indicated that those projects had been eliminated just prior to hearing, the Commission finds that the projected cost of those projects that were included in the costs Bluegrass Water projected would now not be spent at Lake Columbia through the forecasted period as indicated in response to Staff's Second Request, Item 6. Thus, the Commission adjusted the cost of those projects out of CWIP and UPIS for Lake Columbia as shown in Appendix A.

Monitoring Systems. According to the Joint Intervenors, Bluegrass Water is paying a single contractor – Midwest Water Operations, LLC (Midwest) for having a technician visit each system on a daily basis while installing expensive mission control remote monitoring devices.<sup>123</sup> Joint Intervenors add that Bluegrass Water is also paying for the expenses associated with the Mission control subscription and the cost of Midwest's daily

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<sup>123</sup> Brief of the Joint Intervenors at 14.

visits.<sup>124</sup> Joint Intervenors explains that this results in recovery of unnecessarily duplicative costs and the Commission should disallow either the capital or monitoring expenses associated with the mission control system or the costs of Midwest's daily visits.<sup>125</sup>

As discussed in more detail above, the Commission agreed with the argument presented by Joint Intervenors, at least in part, and therefore, found that Bluegrass Water failed to establish the absence of wasteful duplication in this matter with respect to the Mission monitoring system. Thus, as shown in Appendix A, the Commission has included a reduction of \$161,500 in the overall decrease in UPIS to eliminate the capital cost on the Mission control monitoring systems.<sup>126</sup>

Accumulated Depreciation. Bluegrass Water explains that accumulated depreciation consists of the historic total of plant depreciation to date.<sup>127</sup> Accumulated depreciation associated with assets acquired by Bluegrass Water from the prior owners have been carried forward on the books of Bluegrass Water.<sup>128</sup> Bluegrass Water's 13-month average for accumulated depreciation for its sewer system is calculated to be \$2,564,880.<sup>129</sup>

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<sup>124</sup> *Id.* at 14-15.

<sup>125</sup> *Id.* at 15.

<sup>126</sup> See Appendix A.

<sup>127</sup> Application, Exhibit 8, Thies Testimony at 13.

<sup>128</sup> *Id.* at 13-14.

<sup>129</sup> *Id.* at 14.

The depreciation rates that Bluegrass Water proposes to use in this instant case are the same rates approved for affiliates to use in other jurisdictions and are not based on a depreciation study.<sup>130</sup> To evaluate the reasonableness of the depreciation practices of small water and sewer utilities, the Commission has historically relied upon the report published in 1979 by the National Association of Regulatory Utility Commissioners (NARUC) titled *Depreciation Practices for Small Water Utilities* (NARUC Study) and the *O&M Guide for the Support of Rural Water-Wastewater Systems* (O&M Guide). When no evidence exists to support a specific life that is inside or outside of the NARUC and O&M Guide ranges, the Commission has historically used the mid-point of the depreciation ranges to depreciate utility plant.<sup>131</sup>

Bluegrass Water has not presented any supporting analysis or study to show that its depreciation lives are appropriate. Further, because the Commission is adjusting UPIS to reflect plant constructed in 2019, 2020, and the forecasted test-year, accumulated depreciation is being set equal to the depreciation expense for the test year. Given that the Commission's forecasted UPIS is not broken down by account, the Commission is using a composite rate based on the NARUC and the Operation & Maintenance (O&M) Guide depreciation rates.

Applying the NARUC and O&M Guide composite sewer rate of 3.3 percent<sup>132</sup> results in a 13-month average accumulated depreciation balance of \$56,749 which in a decrease to Bluegrass Water's accumulated depreciation of \$2,508,131.

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<sup>130</sup> Responses to Staff's Second Request, Item 2.

<sup>131</sup> Case No. 2020-00195, *Electronic Application of Southeast Daviess County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020).

<sup>132</sup> Responses to Staff's Third Request, Item 7(b).

Cash Working Capital Allowance. Bluegrass Water calculated its cash working capital allowance of \$256,178 by using the 45 day or 1/8th formula methodology, after adjusting for the impacts of Bluegrass Water's proposed adjustments to O&M expenses. While the Commission finds the 1/8th approach to be a reasonable approach for Bluegrass Water, particularly given its size and relative sophistication, and the Commission will permit its use in this matter given those factors, the Commission's cash working capital allowance of \$186,692 reflects the pro forma O&M expense determined reasonable herein.

Contributions In Aid of Construction (CIAC). CIAC carried on the books of Bluegrass Water is from the books and records of the prior owners of the acquired system assets.<sup>133</sup> The forecasted test year reflects additional CIAC that resulted from the system acquisitions approved by the Commission in Case No. 2020-00028 and those acquisitions that will be consummated in Case No. 2020-00297.<sup>134</sup> The 13-month average balance of CIAC Bluegrass Water has included in rate base is \$100,385.<sup>135</sup> Eliminating the CIAC recorded for Delaplain of \$76,684 results in a CIAC of \$23,701.

Based on the adjustments discussed above, the Commission has determined that Bluegrass Water's net investment rate base for its sewer division is \$2,601,721.

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<sup>133</sup> Application, Exhibit 8, Thies Direct Testimony at 15.

<sup>134</sup> *Id.*

<sup>135</sup> *Id.*

	Application 13-Month Average Rate Base	Commission Adjustments	Commission 13-Month Average Rate Base
Rate Base Component - Sewer Utility Plant In Service	\$ 8,438,874	\$ (6,719,196)	\$ 1,719,678
Accumulated Depreciation	(2,564,880)	2,508,131	(56,749)
Net Utility Plant in Service	5,873,995	(4,211,066)	1,662,929
Construction Work In Progress	877,758	(116,034)	761,724
Working Capital Allowance	256,178	(55,409)	200,769
Contributions in Aid of Construction	(100,385)	76,684	(23,701)
Jurisdictional Rate Base	<u>\$ 6,907,546</u>	<u>\$ (4,305,825)</u>	<u>\$ 2,601,721</u>

### Rate Base - Water

Bluegrass Water proposed a forecasted net investment rate base for its water division of \$968,960 based on a 13-month average for that period.<sup>136</sup> In its Base Period Update, Bluegrass Water increased its proposed water rate base to \$1,050,294.<sup>137</sup>

As discussed below in this Order, the Commission has determined that Bluegrass Water's net investment water rate base is \$562,971.

Utility Plant In Service. Bluegrass Water reported a base year UPIS balance of \$1,188,537.<sup>138</sup> According to Bluegrass Water, its base year UPIS balance reflected the

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<sup>136</sup> Responses to Staff's First Request, Item 1, Excel Workbook: [https://www.bguoc.com/Case-Files/2020/Rate-Case-2020/RateBase\\_%28Water%29.xlsx](https://www.bguoc.com/Case-Files/2020/Rate-Case-2020/RateBase_%28Water%29.xlsx); Tab: FY Rate Base - Water B1.

<sup>137</sup> Base Period Update (filed Mar. 19, 2021), Excel Workbook: [BYupdate-RateBase\\_%28Water%29.xlsx](https://www.bguoc.com/Case-Files/2020/Rate-Case-2020/RateBase_%28Water%29.xlsx); Tab: FY Rate Base - Water B1.

<sup>138</sup> Responses to Staff's First Request, Item 1, Excel Workbook: [https://www.bguoc.com/Case-Files/2020/Rate-Case-2020/RateBase\\_%28Water%29.xlsx](https://www.bguoc.com/Case-Files/2020/Rate-Case-2020/RateBase_%28Water%29.xlsx); Tab: FY Rate Base - Water B1.

actual amounts recorded on its books as of August 31, 2020, and the forecasted UPIS additions for the four-month period ending December 31, 2020.<sup>139</sup> Bluegrass Water explained that its 13-month average UPIS of \$1,188,537 was calculated by adding forecasted acquisitions and plant additions and subtracting forecasted retirements through April 2022.<sup>140</sup> However, as noted above with respect to sewer, Bluegrass Water did not actually project any retirements in the forecasted period. Thus, as above, the Commission calculated a 13-month average UPIS to include the construction completed in 2019, 2020, and the forecasted test-year construction using information provided by Bluegrass Water regarding the amounts and timing of proposed project additions provided in response to Staff's Second Request, Item 8. However, for the same reasons discussed above with respect to sewer, the Commission eliminated the proposed remote monitoring costs and the cost of a \$15,000 construction item that Mr. Freeman testified had been eliminated just prior to the hearing. The 13-month average UPIS in the forecast period, as calculated by the Commission, with the monitoring costs and cancelled construction item eliminated, is \$419,882 which is \$768,655 below the forecasted UPIS included by Bluegrass Water in its application. The Commission's calculation of its 13-month average UPIS is included in Appendix A.

Accumulated Depreciation. Bluegrass Water's accumulated depreciation consists of the historic total of plant depreciation to date.<sup>141</sup> Accumulated depreciation associated with assets acquired by Bluegrass Water from the prior owner have been carried forward

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<sup>139</sup> Application, Exhibit 8, Thies Direct Testimony at 13.

<sup>140</sup> *Id.*

<sup>141</sup> Application, Exhibit 8, Thies Direct Testimony at 13.

on the books of Bluegrass Water.<sup>142</sup> Bluegrass Water's 13-month average for accumulated depreciation for its water system is calculated to be \$263,430.<sup>143</sup>

The depreciation rates that Bluegrass Water proposes to use in this instant case are the same rates approved for affiliates to use in other jurisdictions and are not based on a depreciation study.<sup>144</sup> Bluegrass Water has not presented any supporting analysis or study to show that its depreciation lives are appropriate. Further, because the Commission is adjusting UPIS to reflect plant constructed in 2019, 2020, and the forecasted test-year, accumulated depreciation is being set equal to the depreciation expense for the test year. Given that the Commission's forecasted UPIS is not broken down by account it is using a composite rate based on the NARUC.

Applying the NARUC composite sewer rate of 2.82 percent<sup>145</sup> results in a 13-month average accumulated depreciation balance of \$11,667 which in a decrease to Bluegrass Water's accumulated depreciation of \$251,763.

Construction Work In Progress (CWIP). Bluegrass Water defines CWIP as the value of utility plant that is under construction but has not yet been placed into service.<sup>146</sup> Bluegrass Water's forecasted CWIP of \$97,909 is based on a 13-month average of the forecasted balances from April 1, 2021, through April 30, 2022.<sup>147</sup> Using the construction completed in 2019, 2020, and the forecasted test-year construction the Commission

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<sup>142</sup> *Id.* at 13–14.

<sup>143</sup> *Id.* at 14.

<sup>144</sup> Responses to Staff's Second Request, Item 2.

<sup>145</sup> Responses to Staff's Third Request, Item 8.b.

<sup>146</sup> Application, Exhibit 8, Thies Direct Testimony at 13.

<sup>147</sup> *Id.*

calculated a 13-month average CWIP of \$212,036 which is \$114,127 greater than the amount Bluegrass Water’s forecasted. The Commission’s calculation of its 13-month average CWIP is included in Appendix A.

Cash Working Capital Allowance. Bluegrass Water calculated its cash working capital allowance of \$35,266 by using the 45 day or 1/8th formula methodology, after adjusting for the impacts of Bluegrass Water’s proposed adjustments to O&M expenses. While the Commission finds the 1/8th approach to be a reasonable approach for Bluegrass Water, particularly given its size and relative sophistication, and the Commission will permit its use in this matter given those factors, the Commission’s cash working capital allowance of \$32,042 reflects the pro forma O & M expense determined reasonable herein.

Based on the adjustments discussed above, the Commission has determined that Bluegrass Water’s net investment rate base for its water division is \$562,971.

	Application 13-Month Average Rate - Base	Commission Adjustments	Commission 13-Month Average Rate - Base
UPIS	\$ 1,188,537	\$ (768,655)	\$ 419,882
Accumulated Depreciation	(263,430)	251,763	(11,667)
Net Utility Plant in Service	925,106	(516,891)	408,215
CWIP	97,909	114,127	212,036
Working Capital Allowance	35,266	(3,224)	32,042
CIAC	(89,322)		(89,322)
Jurisdictional Rate Base	<u>\$ 968,960</u>	<u>\$ (405,989)</u>	<u>\$ 562,971</u>

### REVENUES AND EXPENSES

Bluegrass Water developed an operating statement for its forecasted test period based on its budgets for the 2020 fiscal year. As required by 807 KAR 5:001, Section 16(6)(a), the financial data for the forecasted test period was presented by Bluegrass Water in the form of pro forma adjustments to its base period, the 12 months ending December 31, 2020. Based on the assumptions built into its budgets, Bluegrass Water calculated its test year water revenues and O&M expenses to be \$90,000 and \$254,014, respectively, and its test year sewer revenues and O&M expenses to be \$1,154,988 and \$2,049,424, respectively. Based on these adjusted revenues and O&M expenses, Bluegrass Water's test period water and sewer operating income (loss) was (\$196,047) and (\$1,176,152).<sup>148</sup> Based on a proposed ROE of 11.80 percent, Bluegrass Water determined that it required a revenue increase of \$336,747 for water and \$2,177,052 for sewer.<sup>149</sup> The Commission will accept components of Bluegrass Water's test period revenue and expenses with certain adjustments discussed below.

#### Direct Expense Adjustments

##### 1. Direct Administrative Expense

In the O&M expenses Bluegrass Water used to calculate its revenue requirement for both sewer and water, Bluegrass Water included a line item labeled "Administrative Services."<sup>150</sup> A breakout of that line item in the work papers for Schedule CE4, as filed

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<sup>148</sup> See Response to Staff's First Request, Item 1, BGUOC2020RateCase-RevenueRequirement\_and\_ConversionFactor\_(Sewer).xlsx; BGUOC2020RateCase-RevenueRequirement\_and\_ConversionFactor\_(Water).xlsx.

<sup>149</sup> *Id.*

<sup>150</sup> See Schedule C-1, Response to Staff's First Request, BGUOC2020RateCase-IncomeStatement\_(Sewer).xlsx, BGUOC2020RateCase-IncomeStatement\_(Water).xlsx.

with Bluegrass Water’s application, indicates that expense consists of “Legal Fees,” “Manage Consult,” and “IT” expenses.<sup>151</sup> The bulk of the Administrative Services expense in the schedules filed with Bluegrass Water’s application was attributable to “Manage Consult” expense (\$39,088 and \$3,066 for sewer and water, respectively, in the base period with \$36,000 and \$6,176 projected for the forecasted period).<sup>152</sup>

When asked to identify who provided the Manage Consult services, the scope of their services, and how those services differed from services provided by CSWR, Bluegrass Water identified PH Enterprises, LLC, Elasticity LLC, and James Fallert Consultant, LLC as providing the services included as Manage Consult expense. Bluegrass Water stated that PH Enterprises provided Utility Operations Consulting and argued that the contract services were needed because PH Enterprises facilitates tap fees for new service connections and CSWR employs no project management staff in Kentucky; that Elasticity provided Communications and Public Relations service and that the service was needed because CSWR employs no public relations professionals; and that James Fallert Consultant provided Legal and Regulatory Consulting and that the service was needed because Mr. Fallert has expertise and decades of experience in regulatory accounting and finance.<sup>153</sup>

In response to subsequent requests for information regarding the specific costs incurred for the direct services provided by PH Enterprises, Elasticity, and James Fallert,

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<sup>151</sup> Response to Staff’s First Request, Item 1 BGUOC2020RateCase-IncomeStatement\_(Sewer).xlsx, BGUOC2020RateCase-Schedule\_CE4.xlsx.

<sup>152</sup> *Id.* at Tab Base & Forecast Detail.

<sup>153</sup> Response to Staff’s Third Request, Item 3.

Bluegrass Water indicated that PH Enterprises provided direct service for its sewer operations for \$2,000 per month from January 2020 through September 2020 for a total of \$18,000; that Elasticity provided direct service for Bluegrass Water from April 2020 through December 2020 at a total cost of \$30,834, and that James Fallert provided direct service to Bluegrass Water's sewer operations in October 2020 totaling \$12,600. In this updated information, Bluegrass Water also indicated that it paid Kentucky Rural Water Association \$550 in December 2020, which Bluegrass Water included as Manage Consult expense.<sup>154</sup> Notably, the sum of what Bluegrass Water later reported as actual Manage Consult expenses in the base period was significantly higher than what Bluegrass Water initially included in Schedule CE4 for the base period.<sup>155</sup>

Joint Intervenors argued that the Commission should closely scrutinize Bluegrass Water's direct contractor expense.<sup>156</sup> Joint Intervenors specifically note that a significant portion of Bluegrass Water's outside expense arises from services provided by Elasticity, and argue that "[t]he majority of the work Elasticity appears to have done for Bluegrass appears to have been promotional in nature."<sup>157</sup> Thus, citing 807 KAR 5:016, Joint Intervenors argue that the expense for Elasticity should be excluded.

In response to Joint Intervenors, Bluegrass Water argued that its expense for Elasticity was reasonable for ratemaking purposes. Bluegrass Water argued that the services offered by Elasticity provide material benefit to its customers. Thus, Bluegrass

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<sup>154</sup> Response to Staff's Fourth Request, Item 9(e), 4-PSC-09(e).xlsx.

<sup>155</sup> See Response to Staff's First Request, Item 1, BGUOC2020RateCase-Schedule\_CE4.xlsx (showing a total Manage Consult Expense for water and sewer of \$42,153);

<sup>156</sup> Joint Intervenors' Brief at 14–15.

<sup>157</sup> *Id.* at 15.

Water argues that those expenses are allowable pursuant to 807 KAR 5:016, Section 3(2).

With respect to expenses attributable PH Enterprises, it is not clear what services PH Enterprises was providing or whether the contract price was reasonable. Bluegrass Water was making payments to PH Enterprises, an apparent affiliate of a previous owner of the Longview/Homestead system, pursuant to the sales contract for the Longview/Homestead system.<sup>158</sup> Moreover, although the sales contract that established the relationship indicated payments would be made based upon work completed, PH Enterprises invoices are numbered “1 of 12” through “12 of 12” and are simply for \$2,000 per month such that they do not appear to be tied to any particular work. Further, the expenses appear to have terminated upon payment of the twelfth of twelve invoices. Thus, the Commission finds that Bluegrass Water failed to establish that the direct expenses for PH Enterprises are reasonable expenses that should be recovered from customers in the forecasted test year (or that they will even be incurred in the forecasted test year).

With respect to the direct expenses for Elasticity, the Commission observes that the detail provided for the specific projects attributed to Bluegrass Water identified in invoices provided does not provide sufficient information to establish that they resulted in material benefit to Bluegrass Water’s utility customers, and the specific projects appear to be one off occurrences e.g. handling the press related to acquisitions and the

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<sup>158</sup> Response to Staff’s Third Request, Item 3, KY2020-290\_BW\_0774- KY2020-290\_BW\_0788 (sale contract provided as contract for services).

production of a video to show some systems before and after construction.<sup>159</sup> Moreover, the work product provided in response to Joint Intervenors' Post-Hearing Request for Information, which consisted in large part of social media posts that were rarely specific to Bluegrass Water customers, would provide little, if any, benefit to Bluegrass Water's customers. There were a few correspondences from Bluegrass Water or CSWR to customers regarding specific issues related to Bluegrass Water's service that Bluegrass Water indicated Elasticity assisted in drafting, but that work appeared to be minimal and the cost of such correspondence were not broken down such that it was impossible to determine what small portion of the cost might be attributable to that work. Moreover, given the expense Bluegrass Water is already paying CSWR for general and administrative work and Bluegrass Water's size, the Commission questions the need for Bluegrass Water to retain an outside public relations firm at a direct cost of over \$30,000 to assist with such matters. Thus, the Commission finds that Bluegrass Water failed to establish that the direct expenses for Elasticity provided material benefit to Bluegrass Water's customers and, therefore, that they are recoverable pursuant to 807 KAR 5:016.

With respect to the direct expenses for James Fallert, it is not clear what services he was providing. The contract Bluegrass Water provided for Mr. Fallert indicated that he was primarily providing services related a rate case,<sup>160</sup> but Mr. Fallert was not offered as a witness in this matter and Bluegrass Water indicated that rate case expense had not

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<sup>159</sup> See Response to Staff's Third Request, Item 3, KY2020-290\_BW\_0803- KY2020-290\_BW\_0826.

<sup>160</sup> Response to Staff's Third Request, Item 3, KY2020-290\_BW\_0827.

been included.<sup>161</sup> Work papers provided by Bluegrass Water also indicate that the expense for Mr. Fallert's services accrued in a single month, October 2020, after Bluegrass Water tendered its application and testimony in this matter.<sup>162</sup> Moreover, CSWR employs a number of accounting professionals, both directly and as contractors, and a portion of their cost is allocated to Bluegrass Water in this matter.<sup>163</sup> Finally, even if the basis for the expense was reasonable and should have been allocated to Bluegrass Water's customers, it is not clear that the expense would reoccur during the forecasted test year given that it accrued in a single month. Thus, the Commission finds that Bluegrass Water failed to establish that the direct expense for James Fallert Consultant is a reasonable expenses that should be recovered from Bluegrass Water's customers in the forecasted test year.

Bluegrass Water projected \$36,000 in Manage Consult expense for sewer and \$6,176 in Manage Consult expense for water in the forecasted period. Bluegrass Water indicated that it projected those expenses based on the expenses incurred in the base period and discussed above.<sup>164</sup> Because the Commission finds that Bluegrass Water failed to establish that the direct expense for PH Enterprises, Elasticity, and James Fallert Consultant are reasonable expenses that should be recovered in the forecasted test year, the Commission must adjust the expenses for Manage Consult expenses in Bluegrass

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<sup>161</sup> Response to Staff's Third Request, Item 24.

<sup>162</sup> Response to Staff's Fourth Request, Item 9(e), 4-PSC-09(e).xlsx.

<sup>163</sup> See Response to Staff's Second Request for Information, Item 1(c), 2-PSC-01c.xlsx (showing \$133,000 in Auditor and Accounting Services in the allocated overhead); Response to Staff's Second Request for Information, Item 14 PSC 2-14 (showing a number of accounting professionals employed by CSWR).

<sup>164</sup> See Response to Staff's Third Request, Item 3(d).

Water's forecasted test year projections. Thus, the Commission will reduce Bluegrass Water's Manage Consult expense for sewer by \$35,450, which reflects amounts paid to the Kentucky Rural Water Association as the only remaining expense, and will reduce its Manage Consult expense for water by \$6,176 to reflect the elimination of any of the expenses discussed above from the projected revenue requirement.

2. Depreciation Expense

Bluegrass Water calculated depreciation expense for the sewer division of \$264,095 by multiplying its proposed depreciation rates by the end of the forecasted period UPIS balances.<sup>165</sup> Even assuming its depreciation rates were supported by the record, Bluegrass Water acknowledged at the hearing that it would be incorrect to apply the rates to the ending balance UPIS in the forecasted period, but rather, acknowledged that the rates should be applied to the 13-month average UPIS balances. Thus, the Commission will adjust Bluegrass Water's depreciation expense to reflect the correct application of the rates to the 13-month average balance.

Bluegrass Water included a negative net salvage value in its depreciation rates, which had the effect of increasing the depreciation rate. However, Bluegrass Water acknowledged that it had not provided specific evidence to support the negative net salvage values.<sup>166</sup> Further, it acknowledged that two of its projects included decommissioning costs for existing plant.<sup>167</sup> The Commission finds that large projects to

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<sup>165</sup> See Response to Staff's First Request, Item 1, BGUOC2020RateCase-RateBase\_(Sewer).xlsx, Tab Dep - FY B3.1 (showing that depreciation expense for a particular account is calculated by multiplying the end of period UPIS by the depreciation rate)

<sup>166</sup> Response to Staff's Third Request, Item 5 and 6.

<sup>167</sup> Response to Staff's Third Request, Item 17.

replace significant plant assets likely also have decommissioning costs baked into the estimates (a utility must “replace” existing plant by removing what is currently there), so Bluegrass Water is seeking to have its customers pay for at least some decommissioning costs of existing plant while also recovering a separate negative net salvage value. Given that the negative net salvage value is not supported by evidence, there is no way to determine if its inclusion under the circumstances will result in duplicative cost recovery or if it is otherwise reasonable. Thus, the Commission finds that Bluegrass Water failed to establish that a negative net salvage value is appropriate in this case.

With respect to the depreciation rates used to calculate depreciation expenses, Bluegrass Water has not presented any supporting analysis or study to show that its proposed depreciation lives are appropriate. Rather, Bluegrass Water indicated that its proposed depreciation rates are based on the rates used by its systems in other jurisdictions.<sup>168</sup> However, Bluegrass Water further indicated that even those rates are not based on a depreciation study, and Bluegrass Water provided no other information to indicate that its proposed depreciation rates are reasonable.<sup>169</sup>

As noted above, when no evidence exists to support a specific life that is inside or outside of the NARUC and O&M Guide ranges, the Commission has historically used the mid-point of the depreciation ranges to depreciate utility plant as discussed above in the

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<sup>168</sup> See Thies Testimony at 16 (indicating that the rates are based on rates used in other jurisdictions); see *also* Response to Staff’s Second Request, Item 2 (indicating that the rates on which Bluegrass Water based its rates are not based on any depreciation study).

<sup>169</sup> See *also* Response to Staff’s Second Request, Item 2 (indicating that the rates on which Bluegrass Water based its rates are not based on any depreciation study).

section discussing accumulated depreciation.<sup>170</sup> The Commission finds that it is appropriate to do so here. However, because Bluegrass Water's UPIS numbers were unreliable and the Commission had to establish a rate base based on projected construction, the UPIS found to be reasonable in this matter is not broken down by account. Thus, the Commission is applying a composite depreciation rate based on the NARUC and the O&M Guide to the 13-month average UPIS.<sup>171</sup>

Applying the NARUC and O&M Guide composite sewer rate of 3.3 percent and removing CIAC amortization of \$7,052 results in a 13-month average depreciation expense of \$49,697 which in a decrease to Bluegrass Water's forecasted depreciation expense of \$214,398. For the water division total depreciation net of CIAC amortization is calculated to be \$11,667 based on the NARUC midpoints, which represents a decrease of \$20,274.

### 3. Operator Contractor Expense

In its application, Bluegrass Water included operating expenses attributed to system operator contracts of \$1,029,348 and \$144,048 for its sewer and water systems, respectively, in the forecast period. The majority of the costs are paid to Midwest.

Joint Intervenors have recommended that Bluegrass Water's system operator contract expense to be reduced to reflect two factors. First, they argue that Bluegrass Water has implemented and is seeking recover the cost for remote monitoring despite

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<sup>170</sup> Case No. 2020-00195, *Electronic Application of Southeast Daviess County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020).

<sup>171</sup> The Commission observes that Bluegrass Water projected depreciation expense for amounts it had not placed in place accounts based on composite rate as well and that such a practice is not uncommon.

paying higher costs to its operator contractor to inspect each system daily. As noted above, Joint Intervenors argue this represents an unnecessary duplication of costs. Second, Joint Intervenors argue that Bluegrass Water confirmed at the hearing that the average cost of the operator agreements is likely to fall at the end of the test year as contracts expire and are renegotiated at a lower rate. Thus, Joint Intervenors propose adjusting all existing contract costs to reflect the cost of the most recently negotiated agreement.

Bluegrass Water responded that because it is required to have operators on site at the systems each day, even with a remote monitoring system in place, it still must comply with this legal requirement and, therefore, the associated expenses should not be disallowed.

The Commission agreed with Joint Intervenors that paying contractors to inspect each system daily as required by the regulation while paying for remote monitoring costs raised questions about duplicative costs. This is why the Commission found that Bluegrass Water failed to prove the absence of wasteful duplication with respect to the remote monitoring equipment and excluded the costs of remote monitoring as discussed above. However, the removal of those costs removes the duplicative costs associated with both monitoring and daily inspections. Thus, the duplicative costs alleged by Joint Intervenors do not justify *also* adjusting Bluegrass Water's operator expense.

Further, the evidence indicates that Bluegrass Water did competitively bid the operator contracts and selected the lowest cost option. The Commission agrees with Joint Intervenors that that the operator contractor costs are likely to fall in the future, as Bluegrass Water indicated that it anticipated. However, the contracts at issue have 2-

year terms such that the first of the four contract terms will not expire until about September 2021. Bluegrass Water could arguable rebid that contract leading up to the end of the term, and there could be savings that the Commission could reflect in this matter, but as with the more recent contracts, Midwest Operators, which won the bids on the earlier contracts, would be the only operator that could take advantage of economies of scale and potentially bid a lower cost.

Greater savings should be achieved in the future by bidding out the operator contracts for all systems together or in groups based on geography as Bluegrass Water indicated it planned to do. If Bluegrass Water rebids its current contracts, which it entered as it purchased systems, based on when the terms expire as opposed to waiting and bidding them in larger groups based on geography, then Midwest Operators will always have an advantage in bidding contracts such that it will not need to lower costs to win the bid. Further, if the Commission forced Bluegrass Water to recognize the savings Midwest Operators are likely to offer if a full open bid took place as each contract expired, then Bluegrass Water would likely be forced to rebid the contracts as they expired to recognize that savings and would thereby be unable to bid all systems at the same the time or based on geography when a number of the contracts have expired. Thus, the Commission finds that an adjustment to operator contract expense would not be appropriate here.

However, the Commission notes that it is making this decision with the understanding that Bluegrass Water will requests bids and proposals from numerous operators for the majority of its systems and for its systems based on geography to allow more operator contractors to take advantage of the economies of scale or regional

benefits when bidding the contracts. The Commission expects that greater savings will be seen in future rate cases.

### Allocated Expense Adjustments

#### 1. Allocation Methodology

Most general and administrative work is performed for Bluegrass Water through its parent company, CSWR, which is managed by an affiliate, Central States. However, CSWR, through Central States, performs general and administrative work for all utilities owned and operated by CSWR and engages in business development activities to acquire additional utilities across the country. Bluegrass Water has no formal cost allocation manual to allocate costs internally between the various affiliates of CSWR and business development activities performed by CSWR.<sup>172</sup>

Bluegrass Water determined the amount of allocated expense for this rate case by first projecting CSWR's "Total SG&A Budget,"<sup>173</sup> which is all of CSWR's budget excluding costs that are allocated directly to a utility affiliate.<sup>174</sup> Bluegrass Water indicated that it then identified and eliminated CSWR's expenses related to business development, referred to as BD Expense in various workpapers,<sup>175</sup> because Bluegrass Water stated "those expenses would provide only marginal benefit to Bluegrass Water."<sup>176</sup> Bluegrass

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<sup>172</sup> Response to Attorney General's First Request, Item 48.

<sup>173</sup> See Schedule OHA1.

<sup>174</sup> Response to Staff's First Request, Item 1(a).

<sup>175</sup> See Schedule OHA1 (showing the elimination of "BD expenses" from the SG&A Budget before Bluegrass Water applied the Massachusetts' method).

<sup>176</sup> Response to Staff's Second Request, Item 1(b) (explaining what "BD expense" is and why Bluegrass Water was seeking to eliminate it).

Water then applied what it referred to as the Massachusetts' method or formula to allocate the remaining expenses between the utility affiliates owned by CSWR or projected to be owned by CSWR in the fourth quarter of 2021.<sup>177</sup>

Bluegrass Water was asked to explain how it determined the BD Expense it excluded from the SG&A Budget, and it indicated that it excluded all of the compensation expense of employees designated specifically as business development employees, because they worked solely on business development activities.<sup>178</sup> Bluegrass Water explained that it then removed a portion of the total compensation expense for three officers, because the officers were involved in supervising the business development employees. Lastly, Bluegrass Water removed a portion of the amounts budgeted as office supply and travel expense in the SG&A budget.<sup>179</sup>

At the hearing, Bluegrass Water was questioned regarding other employees work on business development activities, and it acknowledged that other employees worked on new acquisitions.<sup>180</sup> Bluegrass Water was also questioned regarding why portions of other expense items shown in the SG&A Budget, such as rent, insurance, management consulting, IT consulting, and auditing and accounting consulting, were not allocated to business development. Bluegrass Water was asked to identify portions of other expense items in the SG&A Budget that should have been allocated to business development

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<sup>177</sup> Thies Testimony at 10-11; *see also* Schedule OHA1.

<sup>178</sup> Response to Staff's Third Request, Item 22.

<sup>179</sup> *Id.*

<sup>180</sup> *See* May 19, 2021 H.V.T. at 16:15:14-16:16:53; *see also* May 19, 2021 H.V.T. at 09:14:56-09:22:54.

expense as a post-hearing request for information, but it claimed the only business development expense that was not already allocated was the workers compensation expense for the business development employees.<sup>181</sup>

With respect to the allocation of SG&A Budget after BD Expense is eliminated, Bluegrass Water explained that the Massachusetts formula is based on the ratio of direct labor, capital investment and gross revenue of each affiliate to total direct labor, capital investment and gross revenue.<sup>182</sup> Bluegrass Water asserts that the component factors used in the formula correspond to the significant drivers of general and administrative expense at CSWR.<sup>183</sup> Bluegrass Water asserted, for example, that a higher level of capital investment would require more time and higher expense to perform the necessary accounting procedures to track those fixed assets.<sup>184</sup> For the forecasted test year, as calculated in the application, the Massachusetts' formula produced an allocation percent factor for Bluegrass Water of 5.25 percent, which Bluegrass Water applied to the Total

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<sup>181</sup> Response to Joint Intervenors' Post-Hearing Request, Item 10; see *also* May 19, 2021 H.V.T.

<sup>182</sup> Thies Testimony at 11.

<sup>183</sup> *Id.*

<sup>184</sup> *Id.*

SG&A Budget for the forecasted period,<sup>185</sup> less the amounts Bluegrass Water allocated to business development expense, to determine the amount of allocated overhead that should be assigned to Bluegrass Water.<sup>186</sup>

The Joint Intervenors argue that Bluegrass Water failed to include all business development expenses in determining the amount to be excluded from the SG&A budget before applying the Massachusetts formula. Joint Intervenors assert that Bluegrass Water conceded that it had not taken into account information technology infrastructure, office rents, insurance, legal, and payroll taxes when identifying business development expenses that should be excluded. Joint Intervenors argue that these and any other expenses not related to providing service to Bluegrass Water's customers should be excluded.<sup>187</sup>

Joint Intervenors also argue that the use of the Massachusetts formula to allocate the remaining overhead in this case may not be appropriate based on several factors.

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<sup>185</sup> The Commission notes that in Schedule OHA1, as filed with the application, Bluegrass Water indicated that the total SG&A budget for the forecasted test year was \$11,173,000 and allocated \$4,771,832 of that to BD Expense for a net SG&A budget to be allocated to utility affiliates of \$6,401,169. When Bluegrass Water was asked for a breakdown of the SG&A Budget for the forecasted test year, Bluegrass Water provided an itemized SG&A Budget that totaled only \$7,976,342. See Response to Staff's Second Request, Item 1(c), 2-PSC-01c.xlsx. When Bluegrass Water was asked to identify those portions of \$7,976,342 it would consider to be BD Expense under its methodology, Bluegrass Water identified \$1,194,774 in BD Expense such that the net SG&A budget to be allocated to utility affiliates became \$6,781,568. See Response to Staff's Fourth Request, Item 5, 4-PSC-05.xlsx; see also Response to Staff's Third Request, Item 23 (where Bluegrass Water was unable to provide a breakdown of BD Expense in the forecasted period). Bluegrass Water later explained this discrepancy by stating that the Total SG&A Budget and BD Expense in Schedule OHA1 were projected numbers for 2022, not the forecasted period as indicated, that Bluegrass Water did not project the 2022 budget in sufficient detail to provide any kind of breakdown, and that the itemized SG&A Budget ultimately provided was based on 2021 projections. The Commission will use the projected 2021 SG&A budget when referring to the SG&A budget in the forecasted period going forward, since there is no way to know what is in the 2022 budget, but notes that the discrepancy does raise questions about the accuracy of Bluegrass Water's projections of the SG&A budget, especially given the significant differences.

<sup>186</sup> See Schedule OHA1.

<sup>187</sup> Post-Hearing Brief of the Joint Intervenors at 12.

Joint Intervenors state that Bluegrass Water's Utility Plant in Service balance is low as a percentage of the total system, because this proceeding is the first general rate adjustment sought by Bluegrass Water.<sup>188</sup> Conversely, Joint Intervenors note that Bluegrass Water produces a significantly higher amount of revenue when compared to other companies within CSWR, which Joint Intervenors assert suggests that Bluegrass Water's revenues are proportionately high compared to utility plant of other CSWR companies.<sup>189</sup> Finally, Joint Intervenors reference what they call a redundancy inherent in contracting costs, discussed above in this order, and state that it is not clear if Bluegrass Water's direct labor expenses reflect the true cost of corporate labor to CSWR.<sup>190</sup> Given these factors, Joint Intervenors propose that a better allocation method is one based on Bluegrass Water's total customer connections as a percent of the total connections within CSWR, which results in an allocation percentage of 4.0 percent.<sup>191</sup>

Bluegrass Water asserts that it has allocated common costs appropriately for ratemaking purposes. Bluegrass Water refutes Joint Intervenors' position, stating that the Massachusetts formula remains the most appropriate allocation methodology that allows for a consistent analysis. Bluegrass Water states that using the Massachusetts formula is better than some "arbitrary and unclear 'test' with no basis in the data provided."<sup>192</sup>

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<sup>188</sup> Bluegrass Water's Correction to Test Year Update at 19.

<sup>189</sup> *Id.*

<sup>190</sup> Post-Hearing Brief of the Joint Intervenors at 13.

<sup>191</sup> *Id.* at 14.

<sup>192</sup> Post-Hearing Brief of Bluegrass Water at 10.

Pursuant to KRS 278.2207, “services and products provided to the utility by an affiliate shall be priced at the affiliate’s fully distributed cost but in no event greater than market or in compliance with the utility’s existing USDA, SEC, or FERC approved cost allocation methodology.” Further, “[i]n any formal commission proceeding in which cost allocation is at issue, a utility shall provide sufficient information to document that its cost allocation procedures and affiliate transaction pricing are consistent with the provisions of this chapter.”<sup>193</sup> If a utility has failed to provide sufficient evidence of its compliance, the Commission may “[o]rder that the costs attached to any transaction be disallowed from rates.”<sup>194</sup>

With respect to the allocation of the SG&A Budget between CSWR’s utility affiliates after BD Expense is removed, the Commission agrees with Joint Intervenors that use of the Massachusetts formula is not reasonable under the circumstances. Specifically, due to the nature of CSWR’s business model, CSWR is in the process of purchasing new systems that often have rates that are artificially low and plant that has seen little investment in years. Conversely, Bluegrass Water is proposing significant investment through the forecasted period as well as a rate increase such that Bluegrass Water’s revenue and UPIS could be higher than a comparatively larger CSWR utility simply based on the timing of proposed investment or the rate increase. Additionally, as discussed in more detail above, Bluegrass Water’s UPIS numbers provided in its application are not credible given that Bluegrass Water failed to include retirements in the base and forecasted period, among other things, and Bluegrass Water acknowledged errors in

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<sup>193</sup> KRS 278.2209.

<sup>194</sup> KRS 278.2211(1)(b).

some of the numbers included in its Schedule OHA1, as filed with its application. Thus, while the Massachusetts formula may be appropriate under certain circumstances, perhaps even for Bluegrass Water if CSWR's utility affiliates reach similar or stable places in terms of rates and investment, the Commission finds that Bluegrass Water failed to establish that the Massachusetts formula results in the proper allocation of costs in this matter.

Further, as proposed by Joint Intervenors, the Commission observes that it has often used customer equivalences to allocate general and administrative expenses when a cost of service study (COSS) is not available, as here, and there is not the means to allocate an expense directly. The Commission finds that this method is reasonable under the circumstances given the issues discussed above, and because customer equivalences do provide an estimate of the amount that would be spent providing general and administrative services. In fact, the Commission observes that Bluegrass Water proposed to allocate its portion of the expenses from CSWR between its sewer and water customers using a similar method.<sup>195</sup> Thus, the Commission generally finds Joint Intervenors proposal to use customer equivalents to allocate the SG&A Budget is reasonable.

However, while the Commission is in partial agreement with the Joint Intervenors, it takes issue with the fact that Joint Intervenors allocation based on customer equivalents is based on totals at the end of forecast period. The Commission notes that CSWR's total customer equivalences, what CSWR referred to as connections, changed significantly

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<sup>195</sup> See Schedule OHA1.

during the forecasted period. Bluegrass Water's testimony indicated that at the end of April 2021 CSWR would have approximately 52,605 connections, that it would add approximately 7,000 connections by the end of June 2021, that it would add an approximately 10,200 connections by the third or fourth quarter of 2021, and that it would have approximately 85,000 total connections by the end of December 2021.<sup>196</sup> Based on that evidence, the Commission finds that CSWR will have 52,605 connections at the end of April 2021 and May 2021, 59,605 connections at the end of June 2021, July 2021, and August 2021, 69,805 connections at the end of September 2021, October 2021, and November 2021, and 85,000 connections at the end of each of the remaining months of the forecast period. The Commission finds that a 13-month average, using residential equivalents based on those findings, is a more appropriate method for allocating overhead than the methods proposed by Joint Intervenors or Bluegrass Water. That method yields a sharing percentage of 4.98 percent as shown in Appendix C.<sup>197</sup>

The Commission further finds, as proposed by Bluegrass Water, that expenses arising from business development activities should not be recoverable from utility customers and, therefore, that such expenses should be excluded from the SG&A Budget before it is allocated to utility customers using the sharing methodology identified above. However, the Commission finds that Bluegrass Water failed to establish that its method of identifying and excluding BD Expense is reasonable and results in Bluegrass Water customers paying only the fully allocated cost they should.

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<sup>196</sup> May 19, 2021 H.V.T at 09:12:40; Response to Staff's Fourth Request, Item 12.

<sup>197</sup> Appendix C.

Bluegrass Water itemized the SG&A budget for the forecast period as follows:<sup>198</sup>

Admin & Human Resources	\$	6,320,269
Office Supplies and Travel Expense		682,439
Management Consulting		243,300
Engineering Consulting		20,400
Auditor & Accounting Services		133,000
Legal Fees		87,684
IT		238,250
Rent		168,000
Insurance		77,000
Miscellaneous		6,000
Total Corporate SG&A	\$	7,976,342

Bluegrass Water allocated \$1,097,121 in Admin & Human Resources expense, which Bluegrass Water attributed to the compensation for the business development employees and a portion of the compensation for officers mentioned above, and \$97,653 in Officer Supplies and Travel Expense to BD Expense.<sup>199</sup> Bluegrass Water later indicated that a very small portion of the Insurance expense in the SG&A budget, attributable to the workers compensation of the business development employees, should have been allocated to BD Expense. However, Bluegrass Water indicated that no other portion of the SG&A Budget should be allocated to BD Expense.<sup>200</sup>

The biggest issue with Bluegrass Water's assertion that no other portion of the SG&A Budget should be allocated to BD Expense is that its witnesses acknowledged that other employees worked on business development activities such a portion of those

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<sup>198</sup> See Response to Staff's Second Request, Item 1(c), 2-PSC-01c.xlsx.

<sup>199</sup> See Response to Staff's Fourth Request, Item 5, 4-PSC-05.xlsx; see also Response to Staff's Third Request, Item 23 (where Bluegrass Water was unable to provide a breakdown of BD Expense in the forecasted period).

<sup>200</sup> Response to Joint Intervenor's Post-Hearing Request, 10.

employees work should be excluded.<sup>201</sup> Bluegrass Water also claimed after the hearing that IT expenses for business development activities, presumably only for the employees whose compensation was excluded, were excluded as part of exclusion of travel expense and office supplies, despite not previously indicating that before when asked how BD Expenses was allocated.<sup>202</sup> Bluegrass Water also claimed that no employee classified “exclusively” as a business development employee has a permanent office in CSWR’s building but ignores the officers for which Bluegrass Water excluded a portion of those employees’ compensation as part of business development expense as well as other employees it acknowledged were performing business development activities.

The Commission also observes that CSWR’s business development activities are extensive. As noted above, Bluegrass Water indicated that it had about 52,606 connections as of April 2021 and that it is expected to have 85,000 connections by December 2021. Bluegrass Water has also made additional connections between January 2021 and April 2021, and it indicated that it expected to have about 120,000 connections by end of 2022. Thus, Bluegrass Water was or will be working on about 35,000 new connections at any given time in 2021 and 2022.

If the approximately 35,000 connections Bluegrass Water was or is seeking to acquire at any given time during the forecasted period were part of CSWR, they would represent between about 39.95<sup>203</sup> percent and 29.17<sup>204</sup> percent of CSWR’s total

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<sup>201</sup> See May 19, 2021 H.V.T. at 16:15:14-16:16:53; see also May 19, 2021 H.V.T. at 09:14:56-09:22:54.

<sup>202</sup> See Response to Staff’s Third Request, Item 22.

<sup>203</sup>  $35,000/87,605=39.95\%$

<sup>204</sup>  $35,000/120,000=29.17\%$

connections, based on the numbers used above. Given the process Bluegrass Water described for purchasing systems, and as acknowledged by Bluegrass Water's witnesses, it is clear that personnel other than those explicitly identified by Bluegrass Water are involved in such acquisitions. Moreover, those employees, in turn, use or benefit from resources, such as the building, office supplies, insurance, and legal and consulting services such that portions of those expense items should be allocated to business expenses. Thus, the Commission finds that Bluegrass Water failed to establish that its method of identifying and excluding BD Expense is reasonable and results in Bluegrass Water customers paying only the fully allocated cost they should.

Given that Bluegrass Water has the burden in this matter and on this issue in particular, the Commission could, in its discretion, disallow recovery of the allocated overhead.<sup>205</sup> In lieu of such a result, which likely would not be in the long term interest of Bluegrass Water or its customers, the Commission will treat Bluegrass Water's business development activities as if they are a separate utility with 35,000 connections throughout the forecasted test period and allocate the budget items of the SG&A Budget for the forecasted test year to BD Expense in the same way amounts are allocated above between CSWR utilities. Using that method will result in a sharing percentage of 33.61 percent, which the Commission will apply to the SG&A, except as discussed below, before allocating the remaining SG&A Budget among the utilities as discussed above.

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<sup>205</sup> See, e.g. Case No. 2020-00342, *Electronic Application of CitiPower, LLC for a Rate Adjustment for Small Utilities Pursuant to 807 KAR 5:076*, (Ky. PSC Apr. 27, 2021), Order, at 5-7 (prohibiting recovery in rates of management fee paid to parent company for alleged general and administrative services due to utilities failure to provide proof that the fee is reasonable).

The effect of this change will be discussed below in the summary of the allocated overhead adjustments.

The Commission finds that this method of allocating BD Expense is reasonable, because it is consistent with how the Commission has allocated costs among utility operations in the past when no COSS has been completed and because it is clear from the evidence that Bluegrass Water's business development activities take up significant resources. The Commission also observes that this allocation method results in the Total SG&A Budget being allocated to BD Expenses at a rate roughly between the overall rate Bluegrass Water projected BD Expense would be allocated in the base period, 18 percent,<sup>206</sup> and the calendar year 2022, 42.71 percent.<sup>207</sup>

2. Adjustments to SG&A Budget

a. Admin & Human Resources

In its SG&A Budget for the forecast period, Bluegrass Water included \$6,320,269 for the line item "Admin & Human Resources" in CSWR's SG&A budget.<sup>208</sup> In response to request for information, Bluegrass Water indicated that the only component of this line item is projected employee compensation for CSWR in the forecast period.<sup>209</sup> However, Bluegrass Water also provided a breakdown of employee compensation projected in the forecasted period which indicated the total employee compensation expense would be

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<sup>206</sup>  $\$1,181,221/\$6,580,338=18\%$ . See Schedule OHA1.

<sup>207</sup>  $\$4,771,832/\$11,173,000= 42.71$  percent. See Schedule OHA1; see also Response to Staff's Third Request, Item 23 (indicating those numbers are calendar year 2022 projections).

<sup>208</sup> Response to Staff's Request, Item 1c, Schedule 2-PSC-01c.

<sup>209</sup> Response to Staff's Third Request, Item 11(b).

\$6,083,987.<sup>210</sup> Bluegrass Water did not explain what additional expense, if any, accounted for that difference. Thus, the Commission finds that Bluegrass Water failed to establish that its customers should be responsible for any portion of that difference, and therefore, the Commission reduces the Admin & Human Resources expense in the SG&A Budget from \$6,320,268 to \$6,083,987.

b. New Employee Positions

In response to Staff's First Request, Item 18, Bluegrass Water provided all employee compensation for the forecasted test year broken down by categories of employees. The sum of the total employee compensation for the forecasted period provided in response to that request was \$5,212,209.<sup>211</sup> Staff's Second Request asked Bluegrass Water to identify the employees included in the categories of employees that made up the total compensation for the forecasted period provided in response to Staff's First Request, Item 18. In response, Bluegrass Water provided the spreadsheet referenced above indicating CSWR's total employee compensation projected for the forecasted test year of \$6,083,987.

When asked about the discrepancy in the amounts, Bluegrass Water stated that it was due to the inclusion of eight additional positions in the attachment provided in response to Staff's Second Request that were not in the response provided to Staff's First Request. It indicated two of the positions were labeled as 'Paralegal' and 'O&M IT Specialist' in response to Staff's Second Request and had since been filled. However, it noted that the employees for the other 6 positions were listed only as "New Position,"

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<sup>210</sup> Response to Staff's Second Request, Item 14, PSC 2-14.xlsx.

<sup>211</sup> See Response to Staff's First Request, Item 18, KY2020-00290\_BW\_0078.

because they had not been filled. Bluegrass Water indicated that the positions were not included in response to Staff's First Request, because at the time it responded to that request, on January 29, 2021, it did not know the category into which the employees should be placed. Bluegrass Water stated that the six positions in which the person was identified as "New Position" were simply budgeted positions.<sup>212</sup>

The Commission finds that Bluegrass Water's inclusion of the six "New Position[s]" in the forecasted period is unreasonable because Bluegrass Water failed to establish that the cost would be incurred or that they should be allocated to Bluegrass Water's customers. The Commission observes that six new positions would represent over 13 percent of CSWR's projected employees and officers in the forecasted test year. Yet, at the end of January, when it responded to Staff's First Request, Bluegrass Water could not even place the projected employees in categories as broad as Exempt, Non-Exempt, Director, or Manager, which raises questions regarding why Bluegrass Water was projecting the new employees in the first place. Further, there was no evidence that the employees have been retained. Thus, the Commission finds that Bluegrass Water has not met its burden in establishing that the cost of those employees is an allocated cost for which Bluegrass Water's customers should be responsible and, therefore, further finds that CSWR's Admin & Human Resources expense in the forecasted test period should be further reduced by \$691,141, from \$6,083,987 to \$5,392,846.

c. Health and Dental Insurance

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<sup>212</sup> Response to Staff's Third Request, Item 11.

For both Health and Dental insurance benefits provided to employees, CSWR pays 99 percent of premiums, and the employees pay the remaining 1 percent.<sup>213</sup> In the forecasted test year, for employees not designated as new positions, CSWR included Health and Dental employer contribution totals of \$696,691 and \$35,881, respectively.<sup>214</sup>

The Joint Intervenors proposed a reduction in health and life insurance, citing Commission precedent in the treatment of employee insurance benefit costs.<sup>215</sup> Bluegrass Water objects to the position taken by the Joint Intervenors, stating that each CSWR employee does pay, in part, for the insurance and citing a failure of the Joint Intervenors to reference any applicable decision or guidance.<sup>216</sup>

The Commission has placed greater emphasis on evaluating employee total compensation packages for market and geographic competitiveness to ensure fair rate development and has generally determined that 100 percent employer-funded health and dental care does not meet that criteria.<sup>217</sup> In every general rate case filed since 2016 in which a utility sought to recover its expenses for the payment of 100 percent of its employees' health insurance premiums, the Commission has reduced test year expenses for health insurance premiums to levels based on national average employee contribution

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<sup>213</sup> Response to Staff's First Request, Item 19.

<sup>214</sup> Response to Staff's Second Request, Item 14, Schedule 2-PSC-14 (Confidential).xlsx.

<sup>215</sup> Post-Hearing Brief of the Joint Intervenors at 12.

<sup>216</sup> Post-Hearing Brief of Bluegrass Water at 10.

<sup>217</sup> See, e.g., Case No. 2016-00434, *Application of Shelby Energy Cooperative, Inc. for an Increase in its Retail Rates*, (Ky. PSC July 1, 2017) final Order at 6-7; Case No. 2016-00367, *Application of Nolin Rural Electric Cooperative Corporation for a General Rate Increase*, (Ky. PSC June 21, 2017) final Order at 10-11; Case No. 2016-00365, *Application of Farmers Rural Electric Cooperative Corporation for an Increase in Retail Rates*, (Ky. PSC May 12, 2017) final Order at 6-7; Case No. 2016-00174, *Electronic Application of Licking Valley Electric Cooperative Corporation for a General Rate Increase*, (Ky. PSC Mar. 1, 2017) final Order at 18; Case No. 2017-00349, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates and Tariff Modifications*, (Ky. PSC May 3, 2018) final Order at 19.

rates. The Commission does not see any material difference between a utility paying 99 percent of the premiums and 100 percent of the premiums.

Bluegrass Water was questioned about the Commission's practice of reducing employer contributions for health and dental insurance premiums based on national average contributions. In response, Bluegrass Water argued that as a small company CSWR sees the need to offer best in class compensation and benefits in order to attract the most-qualified employees. Bluegrass Water further argued that "CSWR seeks to attract the most qualified individuals and views total compensation, including the benefits package, as key to achieving that goal."<sup>218</sup>

However, Bluegrass Water acknowledged that CSWR did not look at the typical private sector employer insurance contributions when it was determining what level of contributions for insurance it should provide.<sup>219</sup> Similarly, Bluegrass Water indicated that CSWR, through an outside consultant or otherwise, has not performed a study to compare its wages, salaries, benefits, and other compensation to other similarly-situated companies. Therefore, Bluegrass Water has not substantiated that it took any efforts to plan its compensation "to attract the most qualified individuals." Thus, Bluegrass Water has no evidence to support a finding that its contributions are reasonable and that Bluegrass Water's customers should be responsible for that level of contribution.

It is Commission practice that, in the absence of any compensation policy or benefits study regarding insurance benefits, an adjustment should be made to both health and dental insurance to bring the employee contributions in line with the Bureau of Labor

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<sup>218</sup> Response to Staff's Second Request, Item 24.

<sup>219</sup> *Id.*

Statistics average employer contribution percentages of 21 percent<sup>220</sup> for health and the Willis Benefits Benchmarking Survey 60 percent<sup>221</sup> average contribution for dental insurance. Accordingly, the Commission has reduced CSWR's forecast period employer contributions for Health and Dental insurance by \$139,338 and \$21,248, respectively.<sup>222</sup> Thus, the Admin & Human Resources expense in the SG&A Budget should be further reduced by \$160,586 from \$5,392,846 to \$5,232,260.

d. Increases to Employee Salary

In the forecasted test year, CSWR included \$4,282,377 of salary compensation for employees.<sup>223</sup> At the end of the base year, however, total salary for all positions currently filled at CSWR totaled \$3,918,741.<sup>224</sup> This increase was driven in large part by significant raises projected for several employees, including CSWR's President, who was projected to receive a salary of ██████████ in the base period and a salary of ██████████ in the forecasted test year. Such significant raises are unreasonable on their face, especially

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<sup>220</sup> Bureau of Labor Statistics, Healthcare Benefits, March 2019, Table 10, private industry workers. (<https://www.bls.gov/ncs/ebs/benefits/2019/ownership/private/table10a.pdf>); see also Bureau of Labor Statistics, Healthcare Benefits, March 2018, Table 10, private industry workers. (<https://www.bls.gov/ncs/ebs/benefits/2018/ownership/private/table10a.pdf>) (showing the same percentage contribution rate in 2018).

<sup>221</sup> See Case No. 2019-00109, *Electronic Application of Citipower, LLC (1) for Adjustment of Rates Pursuant to 807 KAR 5:076; (2) Approval for a Certificate of Public Convenience and Necessity to Purchase Pipeline and Other Related Assets; and (3) Approval of Financing*, Order (Ky. PSC Mar. 25, 2020) (citing the The Willis Benchmarking Survey, 2015, at 62-63 [https://www.willis.com/Documents/publications/Services/Employee\\_Benefits/20151230\\_2015WillisBenefitsBenchmarkingSurveyReport.pdf](https://www.willis.com/Documents/publications/Services/Employee_Benefits/20151230_2015WillisBenefitsBenchmarkingSurveyReport.pdf)); see also Case No. 2018-00129, *Application of Inter-County Energy Cooperative Corporation for a General Adjustment of Existing Rates* (Ky. PSC Jan. 25, 2019), Order.

<sup>222</sup> Appendix D.

<sup>223</sup> Bluegrass Water's Response to Staff's Second Data Request, Item 14, Schedule 2-PSC-14 (Confidential).

<sup>224</sup> Bluegrass Water's Response to Staff's Fourth Data Request, Item 6, Schedule PSC 4-6 CONFIDENTIAL.

for a company the size of CSWR. More importantly, Bluegrass Water provided no support for the reasonableness of projecting such raises or why such costs would be necessary. As noted above, Bluegrass Water has not performed any compensation study or analysis to determine the reasonableness of compensation proposed. Bluegrass Water has stated that it does not have a formal compensation policy or criteria, stating that the CSWR leadership “stays attuned to market conditions regarding employment and compensation levels”.<sup>225</sup>

The Commission finds that Bluegrass Water has not met its burden of proof concerning the raises in salary from the end of the base period to the forecast period. In the absence of a supported compensation policy, the Commission finds it is appropriate to adjust salaries in line with the Bureau of Labor Statistics average of a 3.0 percent yearly increase.<sup>226</sup> Applying this to the end of base period rates produces a forecast period salary total of \$4,105,088. Accordingly, the Commission has reduced CSWR’s forecast period Admin & Human Resources by an additional \$177,289<sup>227</sup> from \$5,232,260 to \$5,054,970

e. Auto Allowance

CSWR compensation for its executives includes a yearly auto allowance for certain employees totaling \$102,000 in the forecast period.<sup>228</sup> Bluegrass Water justified the auto

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<sup>225</sup> Response to Staff’s Second Request, Item 23(a); see also Response to Staff’s Second Request, Item 11 (discussion how CSWR decided to provide specific executive salary increases).

<sup>226</sup> Bureau of Labor Statistics - EMPLOYMENT COST INDEX – March 2021 <https://www.bls.gov/news.release/eci.nr0.htm>

<sup>227</sup> Appendix D.

allowance based on extensive travel by the relevant employees.<sup>229</sup> However, a breakdown of CSWR's expense for employee travel to Kentucky indicates the inclusion of mileage payments for employees that received an auto-allowance,<sup>230</sup> which the Commission finds to be duplicative of direct payments made through the auto-allowance such that the auto-allowance payments are unreasonable. Thus, the Commission finds that CSWR's forecast period Admin & Human Resources expense should be reduced by an additional \$102,000 from \$5,054,970 to \$4,952,970.

f. 401(k) Matching

As part of its benefits compensation, CSWR offers a 401(k) retirement plan, with an employer contribution of 3.0 percent of an employee's yearly salary,<sup>231</sup> with an additional 2.0 percent matching of additional employee contributions.<sup>232</sup> The Joint Intervenors state that as CSWR provides bonuses and discretionary 401(k) contributions without a formal criteria or written compensation policy, the total amounts tied to incentive compensation structures should be disallowed.<sup>233</sup> Bluegrass Water refutes the Joint Intervenors assertion that the 401(k) contributions are discretionary, stating that the

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<sup>228</sup> Bluegrass Water's Response to Staff's Second Data Request, Item 14, Schedule 2-PSC-14 (Confidential).

<sup>229</sup> Response to AG's Second Request, Item 10.

<sup>230</sup> See Response to Staff's Fourth Request, Item 7, 04-PSC-07.xlsx.

<sup>231</sup> Bluegrass Water's Response to Staff's Third Data Request, Items 18-19.

<sup>232</sup> May 19, 2021 H.V.T. at 11:24:35, Cox Testimony.

<sup>233</sup> Post-Hearing Brief of the Joint Intervenors at 13.

additional contributions in excess of the base 3 percent are matching and depend on how much an employee chooses to invest.<sup>234</sup>

Concerning the 401(k) contributions, the Commission is in agreement with Bluegrass Water. As there is no discretionary portion of employer 401(k) contributions tied to financial performance, but represents a matching of employee contributions, no adjustment to reduce 401(k) contributions is necessary. However, the effect of adjustments to salaries discussed above will impact the allowable portion of 401(k) contribution in the forecast period. Accordingly, the Commission has reduced CSWR's forecast period Admin & Human Resources by an addition \$8,864 from \$4,952,971 to \$4,944,106.<sup>235</sup>

g. Travel Expense

CSWR included a total overhead Travel Expense of \$576,168 in the forecasted period.<sup>236</sup> As noted above, Bluegrass Water then eliminated a portion of that travel expense as business development expense and allocated a portion of the travel expense to Bluegrass Water based on a sharing percentage. Bluegrass Water did not provide any breakdown of CSWR's total travel expense in historical periods, beyond identifying employees that incurred portions of them, and the total travel expense Bluegrass Water identified for CSWR in historical periods—\$109,830.90, \$314,563.19, and \$271,834.80 in 2018, 2019, and 2020, respectively—were significantly lower than the amount

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<sup>234</sup> Post-Hearing Brief of Bluegrass Water at 10.

<sup>235</sup> Appendix D

<sup>236</sup> Bluegrass Water's Response to Staff's Third Request for Information, Item 12a.

projected in the forecasted test year.<sup>237</sup> Thus, the Commission is not able to find that Bluegrass Water's total projected travel expense in the forecasted test period is reasonable or that the costs should be recovered from Bluegrass Water's customers.

More importantly, Bluegrass Water did provide the actual costs for travel to Kentucky in 2019, 2020, and part of 2021. The records provided show that Bluegrass Water incurred \$26,199 in expense for travel to Kentucky in 2019, \$7,487 in expense for travel to Kentucky in 2020, and \$3,797 in expense for travel to Kentucky in 2021 through at least April 2021 (the records were provided in May 2021 and included costs dated May 2021 such that they must have included part of the cost through May). If the travel expense for employees Bluegrass Water identified as business development employees in each of those years is eliminated, then the records provided by Bluegrass Water show expense for travel to Kentucky in the amount of \$12,714 in 2019, \$4,820 in 2020, and \$3,797 in 2021 through at least April 2021. The Commission observes that the annualized expense for travel to Kentucky in 2021 would be about \$11,392.<sup>238</sup>

The Commission finds that travel expenses allocated to Bluegrass Water should be based on travel to, in, and from Kentucky, because those direct travel expenses will provide a more accurate estimate of costs incurred for the benefit of Kentucky customers. In addition, the Commission finds that the portion of travel expenses attributed to travel by business development employees should be removed in their entirety. Therefore, the Commission has reduced CSWR's forecast period travel expense in the SG&A budget by \$576,168 and directly allocated the allowable travel expense in the amount of \$11,392.

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<sup>237</sup> See Response to Staff's Fourth Request, Item 7, 4-PSC-07.xlsx.

<sup>238</sup>  $\$3,797.34 \times 12/4 = \$11,392.02$

h. Management Consulting

CSWR included Management Consulting expense of \$243,300 in its itemized budget for the forecast test period.<sup>239</sup> Bluegrass Water was asked, among other things, to provide a list of all of the vendors that provided CSWR Management Consulting services in 2019 and 2020, to identify the costs paid to each vendor, and to explain what services CSWR received in consideration for that cost. Bluegrass Water provided a list of vendors used in the base period<sup>240</sup>, but failed to produce an explanation of the services provided by each vendor.<sup>241</sup> Rather, Bluegrass Water identified only broad categories within which the vendors allegedly provided services, including accounting support, system consulting, executive support, human resources consulting, communications and public relations consulting, legal and regulatory consulting, and environmental consulting.<sup>242</sup>

The only Management Consulting vendor for which detailed information was provided was Elasticity, which Bluegrass Water projected would be included both as part of direct expenses and allocated expenses from CSWR. However, as discussed above, Bluegrass Water failed to establish why any portion of the cost for Elasticity should be recovered from Bluegrass Water customers, much less why amounts that cannot be tied directly to Bluegrass Water itself should be recoverable.

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<sup>239</sup> Response to Staff's Second Request, Item 1(c), 2-PSC-01c.xlsx.

<sup>240</sup> Response to Staff's Third Request, Item 12(b).

<sup>241</sup> See Response to Staff's Third Request, Item 12(b)(c); see also May 19, 2021 H.V.T. at 16:20:58; Response to Staff's Fourth Request, Item 7c, 4-PSC-07.xlsx (in which Bluegrass Grass was asked to provide a narrative description of the services provided by contractors but did not do so).

<sup>242</sup> See Response to Staff's Third Request, Item 12(b)(c).

The Commission also notes that it is unclear whether expenses for certain vendors identified as Management Consulting vendors in historical periods were included elsewhere in the SG&A budget. As noted above, Bluegrass Water indicated that vendors provided “Legal and Regulatory Consulting,” “Accounting Support,” and “Environmental Consulting.” However, the SG&A budget for the forecast period includes separate line items for Legal Fees, Auditor and Accounting Services, and Engineering Consulting, which would seem to cover similar services. Bluegrass Water also included expense for Starnik Systems, Inc., which provided IT services, as a Management Consulting expense in 2019, but also included a line item in the SG&A budget explicitly for IT expenses.

The Commission finds that CSWR did not establish that the Management Consulting vendors provide services for which costs should be allocated to Bluegrass Water’s customers. Thus, the Commission finds that the total amount should be disallowed and has, therefore, reduced CSWR’s forecast period Management Consulting Expense in the SG&A budget by \$243,000.

3. Summary of Allocated Overhead Adjustment

The table below reflects the adjustments to the SG&A budget discussed above before business development expense is removed and the SG&A budget is allocated among CSWR’s systems.

Admin & Human Resources	\$	4,944,106
Office Supplies and Travel Expense		106,271
Management Consulting		--
Engineering Consulting		20,400
Auditor & Accounting Services		133,000
Legal Fees		87,684
IT		238,250
Rent		168,000

Insurance		77,000
Miscellaneous		6,000
Total Corporate SG&A	\$	5,780,711

Application of the sharing percentage discussed above for the allocation of business development expense reduces the SG&A budget to be allocated among CSWR’s utilities to \$3,837,897.<sup>243</sup> Application of the sharing percentage discussed above for the allocation of the SG&A budget among CSWR’s utilities results in overhead to be allocated to Bluegrass Water of \$191,136. However, as noted above, the Commission found that travel expense of \$11,392 should be allocated directly. Thus, the Commission finds that overhead allocated to Kentucky should be \$202,519.

In its application, Bluegrass Water projected \$335,961 in allocated overhead for the forecasted test year, of which it allocated \$292,902 to its sewer operations, including the 00297 systems, and \$43,059 to its water operations based on the customer counts of those systems.<sup>244</sup> For the reasons discussed above, the Commission finds that the total allocated overhead should be reduced to \$202,519 in the forecasted period, of which \$176,909 would be allocated to sewer operations and \$25,610 would be allocated to

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Total Adjusted Corporate SG&A	\$	5,780,711
Multiply By: BD Percentage		<u>33.61%</u>
Allocated BD		<u>1,942,814</u>
Total Adjusted Corporate SG&A		5,780,711
Subtract: Allocated BD		<u>1,942,814</u>
Allocatable Corporate SG&A	\$	<u><u>3,837,897</u></u>

<sup>244</sup> See Response to Staff’s First Request, Item 1, BGUOC2020RateCase-Schedule\_OHA1.xlsx.

water operations using Bluegrass Water's allocation methodology.<sup>245</sup> Thus, the Commission finds that the allocated overhead for sewer operations in the forecasted test period should be reduced by \$115,993<sup>246</sup> and that the allocated overhead for water operations in the forecasted test period should be reduced by \$17,449.<sup>247</sup>

#### Adjustment to Remove 2020-00297 Systems

As noted above, the Commission finds that the revenues and costs associated with the 00297 systems should be eliminated when calculating rates and the revenue requirement for the systems at issue here. As discussed above, when determining the rate base for the systems at issue in this case, the Commission did not include any of the elements of rate base for the 00297 systems, such that the return and any taxes on that return only included costs associated with the systems at issue in this case. Further, the Commission applied the depreciation rates discussed above to the rate base that did not include the 00297 systems such that depreciation expense for those systems was not included in the revenue requirement for the systems at issue in this matter.

With respect to sewer expenses or elements of the revenue requirement that were not tied to rate base, namely Bluegrass Water's operation and maintenance expense, the Commission allocated those amounts based on number of residential equivalents provided by Bluegrass Water.<sup>248</sup> The Commission notes that this is the method Bluegrass Water generally used to allocate such expenses when the Attorney General requested a

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<sup>245</sup> See BGUOC2020RateCase-Schedule\_OHA1.xlsx (showing Bluegrass Water's allocation methodology).

<sup>246</sup>  $\$292,902 - 176,909 = \$115,993$

<sup>247</sup>  $\$43,059 - \$25,610 = \$17,449$

<sup>248</sup> Appendix C.

breakdown of rates by system and that such an allocation method would essentially occur by default if the 00297 systems had been included in a unified rate. Moreover, the bulk of Bluegrass Water's expenses or projected expenses were incurred collectively such that they could not be allocated directly. Even operator costs, which is Bluegrass Water's largest expense and arguably could be broken out by contract (the 00297 systems are part of a single contract), are collective, at least in part, because as Bluegrass Water acknowledged at the hearing, the contract costs in the later contracts were lower than the earlier contracts due to the fact that the operator was already providing service to other Kentucky systems. Thus, the Commission finds that allocating the costs not associated with rate base using the customer equivalencies provided by Bluegrass Water is the most reasonable method.

In the forecasted test period, as filed with the application, Bluegrass Water included O&M expenses for sewer totaling \$2,049,424.<sup>249</sup> With the adjustments to Allocated Overhead and Administrative Services line items of the sewer O&M expense discussed above, the sewer O&M expenses were reduced to \$1,898,956. The sharing percentage for the 00297 systems based on the customer equivalent counts projected by Bluegrass Water would be 21.37 percent. Thus, removal of the O&M expenses attributable to the 00297 systems would further reduce the O&M expense for the systems at issue in this matter by \$405,421 to \$1,493,535 as follows:

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<sup>249</sup> Those costs were broken down as follows: Sewer Contractor Operations-\$1,029,348; Sewer Other Operations-\$310,377; Sewer Maintenance-\$112,008; Customer Billing Expense-\$75,237; Uncollectible Accounts-\$8,662; Allocated Overhead-\$292,902; Administrative Services-\$41,122; Property Insurance-\$172,604; Regulatory Expense-\$9,230, and PSC Assessment \$841.00. Response to Staff's First Request, Item 1, BGUOC2020RateCase-IncomeStatement\_(Sewer).xlsx, Tab Inc Statement – SCH C.1.

<u>Category</u>	<u>Sewer O&amp;M- Application</u>	<u>00297 O&amp;M</u>	<u>O&amp;M Systems at Issue</u>
Sewer - Contract Operations	\$1,029,348	\$219,972	\$809,376
Sewer - Other Operations	310,377	66,328	244,049
Sewer - Maintenance	112,008	23,936	88,072
Customer Billing Expense	75,237	16,078	59,159
Uncollectible Accounts	8,662	1,851	6,811
Allocated Overhead	176,909	37,806	139,103
Administrative Services	5,672	1,212	4,460
Property Insurance	172,604	36,886	135,718
Regulatory Expense	6,322	1,351	4,971
PSC Assessment	841	(975)	1816
Total O&M Expenses (Sum of Lines 9-32):	\$1,898,956	\$405,421	\$1,493,535

Uncollectible Accounts.

Applying an uncollectible rate of 0.75 percent to the sewer operating revenues of \$908,166 results in a pro forma Uncollectible expense for the sewer division of \$6,811. Applying the uncollectible rate to the water operating revenues of \$90,000 results in a pro forma Uncollectible expense of \$675 for the water division.

Public Service Commission (PSC) Assessment.

Applying the Commissions assessment rate of rate of 0.20 percent to the sewer operating revenues of \$908,166 results in a pro forma PSC Assessment expense for the sewer division of \$1,816, which is \$975 above the forecasted test-year amount. Applying

the Commissions assessment rate to the water operating revenues of \$90,000 results in a pro forma PSC Assessment expense of \$180 for the water division.

### Interest Synchronization Expense

In its calculation of income tax expense for the sewer division the Commission has included interest expense of \$78,052,<sup>250</sup> based on Bluegrass Water's capital structure, the weighted cost of debt<sup>251</sup> and Bluegrass Water's Rate Base. In its calculation of income tax expense for the sewer division the Commission has included interest expense of \$16,899.<sup>252</sup>

### Income Tax Expense

Using the pro forma operating revenues and expenses for the sewer division determined reasonable herein, the Commission arrives at its pro forma federal income tax expense of (\$113,889), and state income tax expense of (\$28,543). The table below is the Commission's calculation of pro forma income tax expense:

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<sup>250</sup> \$2,601,721 (Rate Base - Sewer) x 3.00% (Weighted Cost of Capital) = \$78,052.

<sup>251</sup> 6% (Long-Term Debt Rate) x 50% (Debt Percentage = 3% (weighted Cost of Debt).

<sup>252</sup> \$562,971 (Rate Base - Water) x 3.00% (Weighted Cost of Capital) = \$16,889.

	Income Tax - Sewer	
	State	Federal
Operating Revenues	\$ 908,166	\$ 908,166
Operating Expenses:		
Operation & Maintenance Exp.	1,493,535	1,493,535
Depreciation	49,697	49,697
General Taxes	13,856	13,856
State Income Taxes	0	(28,543)
Interest Expense	(78,052)	(78,052)
 Total Operating Expenses Before Income Taxes	 1,479,035	 1,450,492
 Taxable Income	 (570,869)	 (542,326)
Multiplied by: Tax Rates	5%	21%
 State and Federal Income Taxes	 \$ (28,543)	 \$ (113,889)

Using the pro forma operating revenues and expenses for the water division determined reasonable herein, the Commission arrives at a pro forma federal income tax expense of (\$25,037), and state income tax expense of (\$6,275). The table below is the Commission's calculation of pro forma income tax expense:

	Income Tax - Water	
	State	Federal
Operating Revenues	\$ 90,000	\$ 90,000
Operating Expenses:		
Operation & Maintenance Exp.	207,125	207,125
Depreciation	(8,607)	(8,607)
General Taxes	92	92
State Income Taxes	0	(6,275)
Interest Expense	16,889	16,889
 Total Operating Expenses Before Income Taxes	 215,499	 209,224
 Taxable Income	 (125,499)	 (119,224)
Multiplied by: Tax Rates	5%	21%
 State and Federal Income Taxes	 \$ (6,275)	 \$ (25,037)

### PRO FORMA ADJUSTMENTS SUMMARY

The effect of the Commission's adjustments on Bluegrass Water's pro forma test-period operations for the sewer division is below. The chart in Appendix E, attached to this Order, is a detailed water pro forma Income Statement that shows the effect of the Commission's adjustments along with the proposed and accepted adjustments of Bluegrass Water for its sewer division.

	Sewer Division		
	Bluegrass Water's Forecasted Test Year	Commission Accepted Adjustments	Commission Adjusted Test Year
Operating Revenues	\$ 1,154,988	\$ (246,822)	\$ 908,166
Operating Expenses	2,331,141	(916,486)	1,414,654
Net Operating Income	<u>\$ (1,176,153)</u>	<u>\$ 669,664</u>	<u>\$ (506,488)</u>

The effect of the Commission's adjustments on Bluegrass Water's pro forma test-period operations for the water division is below. The chart in Appendix F, attached to this Order, is a detailed water pro forma Income Statement that shows the effect of the Commission's adjustments along with the proposed and accepted adjustments of Bluegrass Water for its water division.

	Water Division		
	Bluegrass Water's Forecasted Test Year	Commission Accepted Adjustments	Commission Adjusted Test Year
Operating Revenues	\$ 90,000	\$ -	\$ 90,000
Operating Expenses	286,047	(75,031)	211,016
Net Operating Income	<u>\$ (196,047)</u>	<u>\$ 75,031</u>	<u>\$ (121,016)</u>

### RATE OF RETURN

## Capital Structure

Bluegrass Water proposes a hypothetical capital structure consisting of 50 percent equity and 50 percent long-term debt. The actual capital structure currently approximates 100 percent equity.<sup>253</sup> Bluegrass Water's witness, Jennifer E. Nelson, states that the current capital structure deviates from standard utility practice as it is disproportionately leveraged in favor of equity.<sup>254</sup> She continues stating that the proposed hypothetical capital structure is within industry norms and investor requirements.<sup>255</sup> She avers that although the proposed capital structure is slightly more leveraged than the proxy groups, the proposed hypothetical capital components fall within the proxy group common equity ratios which range from 43.13 percent to 67.12 percent and a mean of 55.23 percent.<sup>256</sup> Additionally, Ms. Nelson notes that the proposed hypothetical capital structure supports the proposed capital structure approved in the acquisition of several assets in Case Nos. 2019-000104 and 2019-00360.<sup>257</sup> Neither the Attorney General nor the Joint Intervenors filed comments regarding the proposed capital structure debt to equity ratios.

The Commission agrees with Ms. Nelson that the current capital structure deviates from standard utility practices and is inappropriate for ratemaking purposes. As noted by Ms. Nelson, David Parcell's text, the *Cost of Capital Manual*, states that there are circumstances where a hypothetical capital structure is used for a utility such as when the

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<sup>253</sup> Direct Testimony of Jennifer E. Nelson, (Nelson Testimony) at 5.

<sup>254</sup> Nelson Testimony at 5.

<sup>255</sup> Nelson Testimony at 7.

<sup>256</sup> Nelson Testimony at 8.

<sup>257</sup> Nelson Testimony at 7.

current capital structure is deemed substantially different from the typical.<sup>258</sup> Ms. Nelson further notes that in *The Regulation of Public Utilities* by Charles F. Phillip, a hypothetical capital structure is used only when the utility's actual capitalization is clearly out of line as compared to others.<sup>259</sup> Clearly a capital structure that approximates 100 percent equity is not typical nor reasonable. Therefore the Commission finds that a hypothetical capital structure consisting of 50 percent long-term debt and 50 percent equity to be reasonable.

### Long-Term Debt Rate

As a component to the hypothetical proposed capital structure, Bluegrass Water proposed a long-term debt rate of 9.50 percent. Ms. Nelson based this debt rate upon the midpoint of then current financing negotiations where the rate was expected to be in the range of 9.00 and 10.00 percent.<sup>260</sup> Ms. Nelson supported a long-term debt rate of 9.50 percent stating that it was reasonable based upon her analysis of the yield curve data on B-rated and CCC-rated utility debt.<sup>261</sup> Ms. Nelson stated that B-rated and CCC-rated utility debt yields are close proxies as they reflect higher risk, below-investment grade utility debt rate costs. As of September 23, 2020, these below-investment grade utility debt yields were in the range of 8.84 to 11.70 percent for terms of 15 years or more. As of January 19, 2021, the range had decreased to 8.42 to 10.63 percent<sup>262</sup> and as of

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<sup>258</sup> Nelson Testimony at 6.

<sup>259</sup> Nelson Testimony at 6–7.

<sup>260</sup> Nelson Testimony at 9.

<sup>261</sup> Nelson Testimony at 9.

<sup>262</sup> Bluegrass Water's Response to Staff's First Request for Information, Item 53.

May 16, 2021, the range had increased, but was still below the range at filing of 8.49 to 11.33 percent.<sup>263</sup>

Bluegrass Water filed notice of financing in Case No. 2021-00128 on March 8, 2021.<sup>264</sup> On April 13, 2021, Bluegrass Water filed a status update in Case No. 2021-00128 and the instant case. In this update, Bluegrass Water stated that due to the Commission's March 24, 2021 Order affirming its decision that any rate adjustment would not include the four systems Bluegrass Water had been approved to acquire in Case No. 2020-00297, the lender was reassessing the situation. Bluegrass Water contends that the reasoning for this reassessment is that even if the current rate case is successful, Bluegrass Water will be in a negative net cash flow position due to the additional acquisitions.<sup>265</sup> Bluegrass Water noted that it was approaching other lenders, but has had indications that financing would not be available due to the impact of the exclusion decision.<sup>266</sup> At the hearing, Mr. Cox stated that Bluegrass Water was working with a St. Louis-based lender and was negotiating financing at a debt rate of 6.00 percent and expected to file with the Commission in the next 20–30 days.<sup>267</sup>

The Attorney General asked that the Commission set a long-term debt rate which accurately reflects current market conditions.<sup>268</sup> The Attorney General notes that Ms.

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<sup>263</sup> BW Hearing Exhibit. 01 filed May 21, 2021.

<sup>264</sup> Case No. 2021-00128, *Electronic Application of Bluegrass Water Utility Operating Company, LLC for Approval of Financing Pursuant to KRS 278:300*, (filed Mar. 8, 2021) Notice.

<sup>265</sup> Case No. 2021-00128, (filed April 13, 2021) Notice: re Status of Proposed Application.

<sup>266</sup> *Id.*

<sup>267</sup> May 19, 2021 H.V.T. at 9:35.

<sup>268</sup> Post-Hearing Brief of the Attorney General at 7.

Nelson's argument that the proposed 9.50 percent long-term debt rate was supported by the argument that the distressed nature of the systems increases the cost of debt is no longer relevant due to the many system improvements illustrated in the video shown by Bluegrass Water at the beginning of the Hearing.<sup>269</sup>

The Joint Intervenors also argued against the proposed 9.50 percent long-debt rate noting that the testimony at the hearing demonstrated that the rate environment for debt has improved since the application filing.<sup>270</sup> The Joint Intervenors supported this position by noting that Bluegrass Water agreed that interest rates for similar situated CCC-rated companies were between 6.00 and 6.97 percent.<sup>271</sup>

Bluegrass Water responded that piecemeal updates, such as to the long-term debt rate, fail to uniformly follow applicable principles.<sup>272</sup> In support of this argument, Bluegrass Water stated that it complied with the law when utilizing a forward-looking test period and updates and/or modifications violate principles of KRS 278.192.<sup>273</sup> Bluegrass Water contends that it provided a full and accurate application in support of the requested rates and not pieces here and there that fail to provide support of the application in full and selecting updates of certain elements upsets the balance contemplated by guidelines used for a forecasted test period.<sup>274</sup> Bluegrass Water maintains that a 9.50 percent long-

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<sup>269</sup> *Id.*

<sup>270</sup> Post-Hearing Brief of Joint Intervenors at 16.

<sup>271</sup> Post-Hearing Brief of Joint Intervenors at 16.

<sup>272</sup> Post-Hearing Response Brief of Bluegrass Water at 7.

<sup>273</sup> Post-Hearing Response Brief of Bluegrass Water at 7.

<sup>274</sup> Post-Hearing Response Brief of Bluegrass Water at 8.

term debt rate reflects the risks associated with small, distressed utilities that have difficulty attracting traditional financing and should not be altered to reflect a lower amount due to perceived fluctuations in the market.<sup>275</sup>

The Commission finds that the rate represented by Mr. Cox of 6.00 percent to be reasonable. The Commission agrees that higher risk utility bonds can be used as a gauge for the determination of the long-term debt rate, but when determining a proxy for the long-term debt rate, the Commission must also assess the current lending market, the regulatory environment, and other comparable investments. Current rates for BBB and CCC rated corporate bonds are 2.410 and 6.974 percent, respectively.<sup>276</sup> These BBB and CCC rated corporate bonds are often referred to as junk bonds or a non-investment grade high risk security. Bluegrass Water's expert, Mr. Dylan D'Ascendis, agreed that utility bonds are issued in a regulated world, hence carry less risk than a low rated corporate bond and thus typically have a lower yield.<sup>277</sup> The Commission-approved 6.00 recognizes the additional risk associated with Bluegrass Water as the 6.00 percent is within the upper range of similar high-risk corporate investments.<sup>278</sup> Further, with a long-term debt rate of 6.00 percent, the Commission recognizes the additional risk of Bluegrass Water as compared to larger utilities in that the rate is greater than the

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<sup>275</sup> Post-Hearing Response Brief of Bluegrass Water at 8.

<sup>276</sup> See May 19, 2021 H.V.T. at 13:50:00 (displaying and discussing bond rates reported by the Wallstreet Journal on May 18, 2021).

<sup>277</sup> May 19, 2021 H.V.T. at 13:30:00.

<sup>278</sup> May 19, 2021 H.V.T. at 14:00:00.

Commission's most recently approved long-term debt rate of 3.89 percent<sup>279</sup> and current forecasted filings of 4.16 percent<sup>280</sup> and 4.04.<sup>281</sup>

### Return on Equity (ROE)

Bluegrass Water proposed a ROE of 11.80 percent. Mr. D'Ascendis' models included the discounted cash flow model (DCF), two risk premium models (RPM), a capital asset pricing model (CAPM), and a comparison of common equity cost rates for a proxy group of domestic, non-price regulated companies based upon the DCF, RPM, and CAPM. Using a proxy group of seven water utilities and forecasted interest rates, the proposed range of equity cost rates were 9.74 to 10.41 percent. Mr. D'Ascendis then applied a business risk adjustment of 1.75% increasing the proposed range to 11.49 percent to 12.16 percent.

In D'Ascendis' evaluation of the capital market, he emphasized that the COVID-19 pandemic has increased risk due to the uncertainty surrounding the full impact and duration of the pandemic.<sup>282</sup> He continued, stating that the increased volatility in the market is the cause of lower bond prices, as opposed to the low interest rate environment, and this same market volatility is contributing to investor's "flight to safety" which creates

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<sup>279</sup> Case No. 2020-00174, *Electronic Application of Kentucky Power Company for (1) A General Adjustment of Its Rates for Electric Service; (2) Approval of Tariffs and Riders; (3) Approval of Accounting Practices to Establish Regulatory Assets and Liabilities; (4) Approval of a Certificate of Public Convenience and Necessity; and (5) All Other Required Approvals and Relief* (Ky. PSC Jan. 13, 2021) at 40.

<sup>280</sup> Case No. 2020-00349, *Electronic Application of Kentucky Utilities Company for an Adjustment of Its Electric Rates, a Certificate of Public Convenience and Necessity to Deploy Advanced Metering Infrastructure, Approval of Certain Regulatory and Accounting Treatments, and Establishment of a One-year Surcredit* (filed Nov. 25, 2020), Application, Direct Testimony of Daniel K. Arbough at 23.

<sup>281</sup> Case No. 2020-00350, *Electronic Application of Louisville Gas and Electric Company for an Adjustment of Its Electric Rates, a Certificate of Public Convenience and Necessity to Deploy Advanced Metering Infrastructure, Approval of Certain Regulatory and Accounting Treatments, and Establishment of a One-year Surcredit* (filed Nov. 25, 2020), Application, Direct Testimony of Daniel K. Arbough at 24.

<sup>282</sup> Direct Testimony of Dylan W. D'Ascendis (D'Ascendis Testimony) at 7.

a situation where utilities are traded similar to the S&P 500 and increase Beta coefficients and investor-required returns.<sup>283</sup> The proposed business risk model is akin to a size premium adjustment and D'Ascendis recommended it based upon Bluegrass Water's size relative to the proxy group.<sup>284</sup> D'Ascendis argued that smaller companies are generally more risky as they face more exposure to business cycles and economic conditions.<sup>285</sup>

Below is a summary of D'Ascendis's models:<sup>286</sup>

**Table 1: Summary of Common Equity Cost Rate**

	<u>Utility Proxy Group</u>
Discounted Cash Flow Model	9.07%
Risk Premium Model	10.88%
Capital Asset Pricing Model	10.96%
Cost of Equity Models Applied to Non-Price Regulated Proxy Group	<u>10.71%</u>
Indicated Range of Common Equity Cost Rates before Adjustment	9.74% - 10.41%
Business Risk Adjustment	1.75%
Indicated Range of Common Equity Cost Rates after Adjustment	<u>11.49% - 12.16%</u>
Recommended Common Equity Cost Rate	<u>11.80%</u>

The Attorney General asked that the Commission refrain from awarding Bluegrass Water a ROE of 11.80 percent and instead set a ROE reflective of current market conditions.<sup>287</sup> The Attorney General argued that the proposed ROE was significantly

<sup>283</sup> D'Ascendis Testimony at 7.

<sup>284</sup> Bluegrass Water's Response to Staff's First Request for Information, Item 45.

<sup>285</sup> D'Ascendis Testimony at 46.

<sup>286</sup> D'Ascendis Testimony at 6.

<sup>287</sup> Post-Hearing Brief of the Attorney General at 5.

higher than the model results, specifically the DCF results of 9.07.<sup>288</sup> The Attorney General noted that the reason for the proposed business risk adjustment of 1.75 percent was business and financial risk and should be disregarded. Regarding business risk, the Attorney General argued that this proposed adjustment ignores that fact that the proxy group utilities face similar legal and regulatory environmental risks and as such, returns associated with business risk are already embedded within the proxy group.<sup>289</sup> He continued, noting that D'Ascendis' arguments regarding regulatory risk were centered around water utilities and not wastewater utilities and thus not applicable since all but one of the systems Bluegrass Water currently operates are wastewater.<sup>290</sup> Finally, the Attorney General argues that D'Ascendis' reasoning that Bluegrass Water's sheer size justifies such an adjustment is not warranted.<sup>291</sup> The Attorney General encouraged the Commission to consider the fact that although Bluegrass Water itself is small, but the parent company is not, and, when setting an appropriate rate of return, the Commission should consider the true scope of the company's operations not simply the capitalization of the relatively new venture in the Commonwealth.<sup>292</sup>

The Joint Intervenors also oppose the proposed business adjustment risk adjustment. They argued that Bluegrass Water has failed to demonstrate that such a premium is necessary to attract investment noting that, to date, Bluegrass Water has not

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<sup>288</sup> Post-Hearing Brief of the Attorney General at 5.

<sup>289</sup> Post-Hearing Brief of the Attorney General at 5.

<sup>290</sup> Post-Hearing Brief of the Attorney General at 5–6.

<sup>291</sup> Post-Hearing Brief of the Attorney General at 6.

<sup>292</sup> Post-Hearing Brief of the Attorney General at 6.

had an issue attracting equity as currently, even though the business plan indicates a loss for a period of time, the utility is fully capitalized.<sup>293</sup> The Joint Intervenors maintained that Bluegrass Water has no analysis to support its contention that its business is any more risky than other similarly situated companies in the market and noted that not only is its product essential but the fact since its customers are primarily residential in nature, a loss of a customer will not result in a significant financial impact.<sup>294</sup>

In response, Bluegrass Water continued its argument that selecting particular rate components, such as the ROE, should be avoided.<sup>295</sup> Bluegrass Water contends that the inclusion of the proposed business risk adjustment and the resulting proposed ROE of 11.80 percent is applicable to a utility such as Bluegrass Water due to its size and risk, such an ROE supported the market conditions when the application was filed and any adjustments in the market since the filing should not be considered.<sup>296</sup>

The Commission agrees that there is additional risk associated with Bluegrass Water, not necessarily because of its size but due to the fact that the utility has acquired small, failing systems that require capital improvements for both regulatory purposes and daily operations. However, a ROE of 11.80 percent is not reflective of the current market conditions. For example, an analysis of a small cap water utility in the April 2021 issue of *Value Line* indicates that in 2019 a ROE of 9.30 percent was earned and 9.90 percent

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<sup>293</sup> Post-Hearing Brief of Joint Intervenors at 16.

<sup>294</sup> Post-Hearing Brief of Joint Intervenors at 16.

<sup>295</sup> Post-Hearing Response Brief of Bluegrass Water at 9.

<sup>296</sup> Post-Hearing Response Brief of Bluegrass Water at 9.

in 2020;<sup>297</sup> and recent Commission awards, although for electric, have been 9.25<sup>298</sup> and 9.30 percent.<sup>299</sup> Further, a business risk or size adjustment has not been approved in the past and the Commission agrees with the Attorney General and the Joint Intervenors that the explicit inclusion is not reasonable as such an adjustment is arbitrary and inflates the model results. The Commission also notes that it does not support Mr. D'Ascendis' indicated range of common equity cost rates where he calculated the low end of the range by taking the average model result and averaging that with the lowest model results. The Commission believes that ignoring low end model results without support for the exclusion purposely inflates the model. Finally, the Commission rejects Bluegrass Water's argument that selecting components of the application and adjusting them violates the principles of a forecasted test year application. In each filed rate case, the Commission evaluates all components which comprise the overall revenue requirement and applies applicable adjustments for which the Commission deems reasonable and results in rates that are fair, just and reasonable.

The Commission finds that a ROE of 9.90 percent for Bluegrass Water to be reasonable in this matter. This ROE is within Bluegrass Water's own models as the

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<sup>297</sup> See Notice of Filing (Ky. PSC Jun. 8, 2021) (containing the relevant pages of The Value Line Investment Survey, Issue 9, Part 2, dated April 9, 2021); see also May 19, 2021 H.V.T. at 14:03:00 (where the pages were discussed at the hearing in confidential session).

<sup>298</sup> See Case No. 2019-00271, *Electronic Application of Duke Energy Kentucky, Inc. for 1) an Adjustment of the Electric Rates; 2) Approval of New tariffs; 3) Approval of Accounting Practices to Establish Regulatory Assets and Liabilities; and 4) All Other Required Approvals and Relief* (Ky. PSC April 29, 2020) at 46.

<sup>299</sup> See Case No. 2020-00174, *Electronic Application of Kentucky Power Company for (1) A General Adjustment of Its Rates for Electric Service; (2) Approval of Tariffs and Riders; (3) Approval of Accounting Practices to Establish Regulatory Assets and Liabilities; (4) Approval of a Certificate of Public Convenience and Necessity; and (5) All Other Required Approvals and Relief* (Ky. PSC Jan. 13, 2021) at 50.

results range from 9.07 to 10.96 percent. The approved ROE also recognizes the unique risk associated with Bluegrass Water's business model, as it is higher than recent awards, but is also reflective of the current economic environment. Much of Mr. D'Ascendis' argument for the proposed ROE range centers around the uncertainty surrounding the COVID-19 pandemic and the resulting volatility.<sup>300</sup> Since the application filing, market volatility, as measured by the VIX substantially leveled and in May 2021, was near the 30-year historical average.<sup>301</sup> Additionally, the uncertainty surrounding the COVID-19 pandemic has been tempered due to the vaccine roll out and the economy re-opening.

#### Rate of Return Summary

Applying the rates of 6.00 percent for long-term debt and 9.90 percent of common equity to the approved capitalization produces an overall cost of capital of 7.95 percent.

### REVENUE REQUIREMENTS

#### Authorized Increase - Sewer

The Commission finds that Bluegrass Water's net operating income for rate-making purposes is \$206,837. We further find that this level of net operating income requires an increase in forecasted present rate revenues of \$959,583.

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<sup>300</sup> D'Ascendis Testimony at 7–13; Bluegrass Water's Response to Staff's First Request, Item 38.

<sup>301</sup> See D'Ascendis' Testimony at 9, where the VIX has averaged 19.39 since 1990 and Bluegrass Water's Response to Staff's Post Hearing Data Request, Item 3 where the May 1, 2021 average monthly VIX was 20.31.

Net Investment Rate Base - Sewer	\$ 2,601,721
Multiplies by: Weighted Cost of Capital	<u>7.95%</u>
Operating Income Requirement	206,837
Less: Operating Income at Present Rates	<u>(506,488)</u>
Operating Income Deficiency	713,325
Multiplied by: Revenue Conversion Factor	<u>1.3452</u>
Increase in Revenue Requirement - Sewer	<u><u>\$ 959,583</u></u>

#### Authorized Increase - Water

The Commission finds that Bluegrass Water's net operating income for rate-making purposes is \$44,756. We further find that this level of net operating income requires an increase in forecasted present rate revenues of \$223,001.

Net Investment Rate Base - Water	\$ 562,971
Multiplies by: Weighted Cost of Capital	<u>7.95%</u>
Operating Income Requirement	44,756
Less: Operating Income at Present Rates	<u>(121,016)</u>
Operating Income Deficiency	165,773
Multiplied by: Revenue Conversion Factor	<u>1.3452</u>
Increase in Revenue Requirement - Water	<u><u>\$ 223,001</u></u>

#### Unified Rate

Bluegrass Water proposes a unified, monthly flat rate for all residential wastewater customers, multi-family, and commercial customers based on a residential equivalency of \$96.14, \$72.11, and \$240.36, respectively.<sup>302</sup> For its water customers, Bluegrass

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<sup>302</sup> Application Exhibit 3.

Water proposes to increase the current monthly flat rate from \$22.79 to \$105.84.<sup>303</sup> The proposed monthly flat rate design was adopted by Bluegrass Water as it mimics the rate design of the former individual systems it acquired.<sup>304</sup>

The Attorney General did not provide comments concerning the proposed unified monthly flat rate design but did request that such a large rate increase be phased in gradually to minimize rate shock.<sup>305</sup>

The Joint Intervenors argue that the proposed unified rate design for the wastewater customers creates unfair subsidization.<sup>306</sup> Customers of systems that need little or no capital expenditures to maintain proper service will subsidize the major repairs and rehabilitation of the distressed systems Bluegrass Water has acquired. The Joint Intervenors state that a unified rate may be an appropriate goal over time; however, it is unfair, unjust and unreasonable to move to a unified rate in a single proceeding.<sup>307</sup> The Joint Intervenors propose a limiting factor to the amount of any single system's capital expense can be shared with customers from other systems, which can then be revised in subsequent cases.<sup>308</sup> Bluegrass Water argues that eventually each of the systems will require significant capital investment; therefore, the customers are better served by the

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<sup>303</sup> *Id.*

<sup>304</sup> Application at 5.

<sup>305</sup> Post-Hearing Brief of Attorney General at 8.

<sup>306</sup> Post-Hearing Brief of Joint Intervenors at 17.

<sup>307</sup> *Id.*

<sup>308</sup> *Id.*

proposed unified rate.<sup>309</sup> Bluegrass Water states the proposed unified rate will allow for the financial burdens common to all systems to be distributed in a beneficial manner to each of the ratepayers, and allow the systems—which are historically distressed—to be brought into and kept in compliance and to continue providing safe and reliable service.<sup>310</sup> Bluegrass Water states that the Commission has consistently supported a unified rate structure to encourage consolidation of systems to improve the quality of service in the Commonwealth.<sup>311</sup>

The Commission supports the principle that utility rates should be cost based, and that in most circumstances each class of utility ratepayers should pay the costs which the utility incurs to provide that class with utility service. The majority of Bluegrass Water’s customers are in the residential class. A separate rate for each geographically distinct merged system of Bluegrass Water would create unreasonable and undue hardship to individuals in some areas served by Bluegrass Water. The Commission finds that the proposed unified monthly flat rate design, with wastewater multi-family dwellings and commercial customers monthly rates based on residential equivalency, should be approved for Bluegrass Water’s customers.

#### Nonrecurring Charges

The Commission has reviewed Bluegrass Water’s current and proposed Nonrecurring Charges for both the water operations and the sewer operations. Bluegrass

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<sup>309</sup> Cox Testimony at 72–73.

<sup>310</sup> Post-Hearing Response Brief of Bluegrass Water at 7.

<sup>311</sup> *Id.*

Water has not provided cost justification supporting the current charges or the proposed charges for either water operations or the sewer operations.<sup>312</sup> In support of these charges, Bluegrass Water states that the new Nonrecurring Charges are to recover costs incurred by Bluegrass Water. For the current Nonrecurring Charges, Bluegrass Water maintains that the previous utility instituted these and they do not know what cost justification was presented when the charges were established.<sup>313</sup> In addition, Bluegrass Water did not provide any forecasted occurrences for the current Nonrecurring Charges for water customers or proposed Nonrecurring Charges for sewers customers as requested.<sup>314</sup> Because no costs have been identified in support of these Nonrecurring Charges, the charges have been reduced to zero. If Bluegrass Water desires to charge Nonrecurring Charges in the future, Bluegrass Water should file a request through the Commission's Electronic Tariff Filing System and provide all cost justification and supporting documentation for these charges.<sup>315</sup>

### Tap Fees

Bluegrass Water proposed a Tap Fee for all of its sewer systems of \$750.00. Currently, Bluegrass Water charges Tap Fees for four sewer systems: Arcadia Pines, \$500.00; Great Oaks, \$750.00; Golden Acres, \$250.00; and Marshall Ridge, \$500.00. Bluegrass Water has a Water Tap Fee of \$350.00 and has not requested to adjust this fee in its application. Like the non-recurring charges, Bluegrass Water did not provide

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<sup>312</sup> Staff's Fourth Request for Information (filed Apr. 29, 2021), Items 1 and 3.

<sup>313</sup> Bluegrass Water's Response to the Commission Staff's Fourth Request for Information (filed May. 29, 2021), Items 1 and 3.

<sup>314</sup> *Id.*, Items 2 and 4.

<sup>315</sup> See, 807 KAR 5:011, Section 10.

cost justification for either the current Water Tap Fee or the proposed Sewer Tap Fee, and maintained that the proposed Tap Fees recover only a fraction of the costs incurred by Bluegrass Water.<sup>316</sup> The Commission finds that the proposed Sewer Tap Fee of \$750.00 should be denied; but, the current tariffed Water and Sewer Tap Fees should be allowed to continue to be charged. If Bluegrass Water desires to charge a unified Sewer Tap Fee, Bluegrass Water should file a request through the Commission's Electronic Tariff Filing System and provide all cost justification and supporting documentation.

### SUMMARY

The Commission, after consideration of the evidence of record and being otherwise sufficiently advised, finds that:

1. The rates set forth in Appendix B to this Order are the fair, just and reasonable rates for Bluegrass Water to charge for service rendered on and after the date of this Order.

2. The rate of return granted herein is fair, just and reasonable and will provide sufficient revenue for Bluegrass Water to meet its financial obligations with a reasonable amount remaining for equity growth.

3. The rates proposed by Bluegrass Water would produce revenue in excess of that found reasonable herein and should be denied.

IT IS THEREFORE ORDERED that:

1. Bluegrass Water's request for a declaratory order finding that the construction on Airview's wastewater treatment facility; the project to replace Brocklyn's wastewater treatment facility; construction on Delaplain's wastewater treatment facility;

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<sup>316</sup> *Id.*, Item 3.c.

construction on River Bluffs' wastewater treatment facility; and construction of the Mission monitoring systems is denied based on the Commission's finding that a CPCN is or was required for that construction.

2. The Commission, exercising its discretion pursuant to 807 KAR 5:001, Section 19(1), declines to make a specific finding regarding whether each additional construction item proposed by Bluegrass Water requires a CPCN and, therefore, denies Bluegrass Water's request for a declaratory order finding that those construction items do not require CPCN.

3. Bluegrass Water's request for a CPCN is granted with respect to the construction on Airview's wastewater treatment facility that has not been completed, and it is denied with respect to the construction that has been completed.

4. Bluegrass Water's request for a CPCN is denied with respect to the project to replace Brocklyn's wastewater treatment facility; construction on Delaplain's wastewater treatment facility; construction on River Bluffs' wastewater treatment facility; and construction of the Mission monitoring systems.

5. The rates and nonrecurring charges proposed by Bluegrass Water are denied.

6. The rates in Appendix B to this Order are approved for service rendered by Bluegrass Water on and after the August 1, 2021 for the systems at issue in this matter.

7. The rates of the 00297 systems shall continue to be charged in accordance with the tariffs sheets for those systems filed on or about April 5, 2021, until a subsequently filed tariff proposing to amend those rates is filed pursuant to KRS Chapter 278 and 807 KAR Chapter 5.

8. Within 20 days of the date of this Order, Bluegrass Water shall file with the Commission, using the Commission's Electronic Tariff Filing System, new tariff sheets setting forth the rates, charges, and revisions approved herein.

9. Bluegrass Water's March 22, 2021 motion for an enlargement of time to March 26, 2021, to respond to the Commission's Staff's Third Request for Information is granted.

10. Absent a request for rehearing, this case will be closed and removed from the Commission's docket upon expiration of the statutory time period to request rehearing.

By the Commission

Vice Chairman Kent A. Chandler  
dissenting in part



ATTEST:

  
\_\_\_\_\_ for  
Executive Director

Case No. 2020-00290

**Opinion of Vice Chairman Kent A. Chandler in Case No. 2020-00290, Concurring  
In Part and Dissenting In Part**

Although I appreciate the Majority's well-written and exhaustive Order, particularly given the complexity of the matter before us, I must write separately to dissent in significant part regarding the Order's conclusion and rates. Before explaining the reason for which I dissent, I note that I concur on a number of items in the Majority's Order. I concur with the Majority insofar as they reaffirm the Commission's previous decisions denying the inclusion of the 00297 systems as part of this request to increase rates.<sup>1</sup> I also concur with the Majority's decision regarding "Procedural Issues."<sup>2</sup> Finally, I find no error with the Majority Order's determinations with regard to Certificates of Public Convenience and Necessity and the adoption of a unified tariff, generally.<sup>3</sup>

Regretfully, my ability to concur with the Majority's Order ends there. Instead of approving the rates found in the Majority's Order as fair, just and reasonable, I would have voted to order no change to Bluegrass Water's present rates, due to the utility's failure to (1) provide reasonable, sufficient or competent financial information, (2) provide the information necessary to appropriately calculate a revenue requirement, and (3) generally meet its burden of proof as to its proposed rates. Although Bluegrass Water is aware of the components of rate base<sup>4</sup> and how to calculate it, including the calculation

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<sup>1</sup> Majority Order at 3-4, 10-13. See also March 24, 2021 Order denying Bluegrass Water's Motion to Alter the Commission's 2/12/21 Order; February 12, 2021 Order denying Bluegrass Water's November 18, 2020 Motion for Deviation from Requirements relating to Customer Notice.

<sup>2</sup> Majority Order at 14-15.

<sup>3</sup> *Id.* at 15-38.

<sup>4</sup> Direct Testimony of Brent G. Thies at 12-13.

of Utility Plant in Service (UPIS),<sup>5</sup> as the Majority's Order discusses, the information provided by the utility was incomplete, contrary to other sources, and wholly deficient for purposes of determining rate base. Bluegrass Water failed to provide a reasonable or competent amount for UPIS by failing to reflect any amount for asset retirements,<sup>6</sup> and failing to adequately explain discrepancies in its forecasted CWIP and UPIS calculations.<sup>7</sup> Rate base is of course a foundational component of the calculation of a utility's revenue requirement. Net investment rate base is necessary to determine a utility's operating income and depreciation expense. With a net investment rate base of \$0, for instance, a utility's revenue requirement is equal to operating expenses, while the operating expenses would include no depreciation expense. Once it was concluded that Bluegrass Water had not provided competent support or explanation for the determination of rate base, I would have found the application deficient to the point fair, just and reasonable rates could not be determined from the record. This determination would be in accordance and pursuant to KRS 278.190(3), wherein the controlling statute clearly notes "the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the utility." Failure by the utility to meet its burden of proof should result in no increase in rates.

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<sup>5</sup> *Id.* at 12-15.

<sup>6</sup> See Majority Order at 44-46, wherein the majority notes that the "undisputed evidence indicates Bluegrass Water did not include any retirements in the base period, the forecasted test year, or the period between the base and forecasted periods despite providing sworn testimony with its application that it had done so," and the Majority Order goes on to discuss why doing so was results oriented to the utility's benefit and was unreasonable.

<sup>7</sup> Majority Order at 44.

Nevertheless, the derivation and presentation of rate base is not the only issue for which I would have determined the utility failed to meet its burden of proof regarding its proposed rates. Bluegrass Water provided incorrect or inconsistent amounts for depreciation<sup>8</sup>, Business Development,<sup>9</sup> and “Admin and Human Resources” expenses.<sup>10</sup> Bluegrass Water’s compensation is unreasonable, unsubstantiated and lacks and formal policy.<sup>11</sup> The only basis provided for current levels of compensation or for increases, including CSWR’s CEO’s nearly 30% raise, was contradicted by the evidence of record.<sup>12</sup>

During the pendency of this matter Bluegrass Water has spent significant time, effort, and expense explaining its inconsistent or incomplete case record. Nearly all of these issues are related to the organization’s finances or management, not necessarily Bluegrass Water’s prosecution of the case. Bluegrass Water is the master of its petition. It chose when and how to file its application in this matter. It further determined the water and wastewater systems it sought to purchase, and after purchase, the amount of investment it intended on making before, during, and after its proposed test year; a time period the utility was further in control of determining in its application. Bluegrass Water came into the Commonwealth claiming it intended to “professionaliz[e] distressed”

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<sup>8</sup> Majority Order at 46, 66-67.

<sup>9</sup> Majority Order at FN 183.

<sup>10</sup> Majority Order at 82-83.

<sup>11</sup> Majority Order at 86, FN 217 citing Bluegrass Water’s Response to Commission Staff’s Second Request, Item 24.

<sup>12</sup> See Majority Order at 86-87, stating “Bluegrass Water further argued that ‘CSWR seeks to attract the most qualified individuals and views total compensation, including the benefits package, as key to achieving that goal,’” while later noting CSWR did not review peer employers when determining employer insurance contributions and that neither Bluegrass Water nor CSWR “performed a study to compare its wages, salaries, benefits, and other compensation to other similarly-situated companies.”

utilities. As explained herein and as detailed in the Majority's Order, the support provided for the utility's proposed application and rate increase failed to satisfy Bluegrass Water's burden of proof and falls short of what should be expected from an organization of Bluegrass Water's stature. It should not fall to the utility's attorney or the Commission to rectify or explain away an applicant's material shortcomings related to the financial information provided as support for a rate increase.

Finally, with regard to Bluegrass Water and this application, I must note that none of the systems owned by the utility now was without issue at their time of transfer to Bluegrass Water. A few of the orders approving either the transfer of jurisdictional systems to Bluegrass Water or the initiation of service under KRS 278.020 of previously non-jurisdictional systems indicated the problems or condition of the current service. The Majority's Order discussed this reality in sections, noting the obligation of Bluegrass Water to enter into Agreed Orders with the Commonwealth's Energy and Environment Cabinet to cure identified deficiencies. Upon review of the systems Bluegrass Water has acquired over the past two years, I would note that most of them are older, in poor operating condition, have generally lacked recurring maintenance and require (or have required for years) significant capital investments to provide adequate service. Regardless of who purchased many of these systems, rehabilitations will need to be made in order to continue providing service. Given the size of those systems, some sort of consolidation or regionalization is likely necessary to simultaneously provide adequate service at affordable rates. I take no position on Bluegrass Water's business model at this time, but I would note that to-date I have yet to see the type of "economies of scale

and scope that can sustain and improve existing service” and a rate that appears to me as being fair, just or reasonable.<sup>13</sup>

I further write today to explain the systemic shortcomings this case has served to elevate. During the pendency of this matter, the Commission received a number of comments on the application, including those from elected officials. Public comments ranged from general concern about the ability to pay for the proposed increase, to questions of whether investments underlying the rate increase were reasonable or necessary. Many of the comments request the Commission take specific action on the application, such as considering the affordability of the proposal or the sheer increase of the application. As a practical matter, two factors are at play that complicate the Commission’s ability to make much meaningful impact on applications like the one at hand, short of a finding the utility merely has not met its burden of proof. Regretfully, these two factors exacerbate one another.

The first complicating factor is the lack of evidence before us. Short of finding an applicant has failed to meet their burden of proof, the Commission often depends on record evidence other than the applicant’s to make findings of fact contrary to the utility’s proposal. In this matter, neither intervening party, the Attorney General,<sup>14</sup> nor the Joint

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<sup>13</sup> Verified Joint Application for Approval of Acquisition and Transfer of Ownership and Control of Utility Assets, Case No. 2019-00104 (Apr. 16, 2019) at 23.

<sup>14</sup> These statements should not be construed as a critique of the Attorney General’s Office of Rate Intervention (ORI), or the Attorney General. My personal experience and understanding is that the resources available for the purpose of participating before the Commission have been limited for decades. The Attorney General’s ORI has historically been staffed exclusively by attorneys, rather than staff rate experts that can offer testimony. Further, consultant witnesses that have experience in rate matters are not inexpensive. Again, these comments are merely illustrative of a current example. The Attorney General’s ORI has occasionally experienced the same resource constraints as I detailed for the Commission below.

Intervenors provided much in the way of alternative evidence. This is not to say that either of the parties failed to play a meaningful role in the matter. Indeed, the Majority's Opinion cites a number of arguments made by both parties that it agreed with, and cited a number of times to responses to intervenor discovery requests in support of its conclusions and rationale. However, discovery and arguments can only go so far in determining fair, just and reasonable rates. Evidence is the lifeblood of administrative decisions, including those made by this Commission. One needs only review the statute and case law in regard to judicial review of Commission orders to appreciate the importance of evidence. Commission orders may only be vacated or set aside if they are found to be unreasonable or unlawful, and an order is unreasonable "only if it is determined that the evidence presented leaves no room for difference of opinion among reasonable minds."<sup>15</sup> Without contrary "affirmative" evidence, such as intervenor testimony, and other than a finding the applicant failed to meet its burden of proof, the Commission is limited in its ability to effectuate much change in an applicant's proposed rates. The only additional tool the Commission has at its discretion is its experience, case precedence and dedicated staff. Staff and Commission resources though are not what they used to be.

The Commission currently has approximately 70 employees, including the Commissioners. These employees include those that actively and substantively work on open matters, like financial analysts and attorneys, as well as staff that support the Commission's work, such as IT professionals and consumer service representatives. In

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<sup>15</sup> KRS 278.410; *Kentucky Industrial Utility Customers, Inc. v. Kentucky Utilities Company*, 983 S.W.2d 493, 499, citing *Energy Regulatory Commission v. Kentucky Power, Ky. App.*, 605 S.W.2d 46 (1980).

cases such as this one, the Commission depends on its staff to help investigate the reasonableness of the application. Commission Staff's work on these cases is invaluable, and their efforts are exactly what the General Assembly envisioned decades ago in providing the Commission an opportunity to have full-time staff that work exclusively on utility matters. Specifically, the Commission is authorized by the following statute to hire and employ competent staff to help it "perform the duties and exercise the powers conferred by law upon the Commission,"<sup>16</sup> including limiting the rates charged by utilities to only those that are "fair, just and reasonable."<sup>17</sup>

The commission acting through the executive director may employ such clerks, stenographers, rate experts, agents, special agents, engineers, accountants, auditors, inspectors, lawyers, hearing examiners, experts and other classified service employees and the commission may contract for services of persons in a professional or scientific capacity to make or conduct a hearing or a temporary or special inquiry, investigation or examination as it deems necessary to carry out the provisions of this chapter, or to perform the duties and exercise the powers conferred by law upon the commission.<sup>18</sup>

Nevertheless, in the absence of the "affirmative" evidence discussed above, the Commission depends more and more on its Staff to help investigate and analyze whether applications should approved, modified or revoked. Outright approval or denial of a proposal poses fewer complications than that of a modification, which are ordinarily made in the public interest. The Commission could outright revoke every petition before it that has a minor issue or concern, indicating the reason for denial with an opportunity for the

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<sup>16</sup> KRS 278.110.

<sup>17</sup> KRS 278.030.

<sup>18</sup> KRS 278.110.

applicant to refile. Doing so though would cause untold inefficiency and ultimately not result in any public benefit. Therefore, the Commission has for decades, likely since its inception, made material and substantive modification to proposals in order to ultimately grant their approval. This has proven to be effective and efficient. Nevertheless, without “affirmative” evidence, the Commission depends on its and its Staff’s expertise and experience to examine whatever evidence is in the record in order for the Commission to say what is fair, just and reasonable when a proposal before it is facially unfair, unjust or unreasonable. The problem the Commission finds itself in is that with more cases, and more complicated cases, coming before us, we have less staff than ever. During fiscal year 2013, for instance, the Commission employed an average 88 individuals with a personnel funding cap of 98 positions. As noted above, today we find ourselves with approximately 70 staff members, with a funding cap of 76 positions. Frankly, each year the Commission Staff is asked to do more with less.

It is cases like this that the lack of “affirmative” evidence by intervenors and the strain on Commission Staff is most evident. The Majority’s Order in this case is as long, or longer than, investor-owned electric and gas rate case orders for utilities with tens-of-thousands of customers and hundreds-of-millions of dollars in annual revenues. This is a complicated case. Without intervenor testimony, for instance, the Commission is limited in its ability to make a meaningful effort to ensure rates are fair, just and reasonable. The Commission cannot merely dismiss a proposal as being “too high,” or result in rates that are “unaffordable,” particularly given that neither assertion is supported by record evidence. The issue is not KRS Chapter 278 either. The statutes the Commission operates under are adequate on this topic. The issue, insofar as commenters and the

public seek to have the Commission play a more active role in ensuring rates are fair, just and reasonable, or service is adequate, efficient and reasonable, is a lack of resources. More resources must be dedicated to (1) providing as much evidence as possible for the Commission to consider and (2) ensuring the Commission and its Staff have the time and personnel to investigate and adjudicate proposals and make decisions in the public's interest. This can be accomplished in a number of ways, including funding, subject to Commission approval, of intervenor witness expense and merely increasing Commission Staff counts to previous levels.

Vice Chairman Kent A. Chandler  
dissenting in part

ENTERED  
AUG 02 2021  
bsb  
KENTUCKY PUBLIC  
SERVICE COMMISSION

ATTEST:



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Executive Director

Case No. 2020-00290

## APPENDIX A

### APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2020-00290 DATED AUG 02 2021

13-Month Average UPIS - Sewer

	Total Estimated Project Budget	Estimated Project		13-Month Average UPIS - Sewer												13-Month Average UPIS		
		Start Date	End Date	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21	Jan-22	Feb-22	Mar-22		Apr-22	
Air view	\$ 325,436	Sep-20	Sep-21	-	-	-	-	-	\$ 325,436	\$ 325,436	\$ 325,436	\$ 325,436	\$ 325,436	\$ 325,436	\$ 325,436	\$ 325,436	\$ 325,436	\$ 200,289
Monitoring System	\$ (10,000)	Sep-20	Sep-21	0	0	0	0	0	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(6,154)
Brooklyn	266,388	Sep-20	Sep-21	266,388	266,388	266,388	266,388	266,388	266,388	266,388	266,388	266,388	266,388	266,388	266,388	266,388	266,388	266,388
Monitoring System	(10,000)	Sep-20	Sep-21	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)
Fox Run	232,660	Sep-20	Sep-21	0	0	0	0	0	232,660	232,660	232,660	232,660	232,660	232,660	232,660	232,660	232,660	143,175
Monitoring System	(22,000)	Sep-20	Sep-21	0	0	0	0	0	(22,000)	(22,000)	(22,000)	(22,000)	(22,000)	(22,000)	(22,000)	(22,000)	(22,000)	(13,538)
Kingswood	101,764	Sep-20	Sep-21	0	0	0	0	0	101,764	101,764	101,764	101,764	101,764	101,764	101,764	101,764	101,764	62,624
Monitoring System	(11,000)	Sep-20	Sep-21	0	0	0	0	0	(11,000)	(11,000)	(11,000)	(11,000)	(11,000)	(11,000)	(11,000)	(11,000)	(11,000)	(6,769)
Lake Columbia	216,005	Sep-20	Sep-21	0	0	0	0	0	216,005	216,005	216,005	216,005	216,005	216,005	216,005	216,005	216,005	132,926
Monitoring System	(10,000)	Sep-20	Sep-21	0	0	0	0	0	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(6,154)
Canceled Projects	(85,000)	Sep-20	Sep-21	0	0	0	0	0	(85,000)	(85,000)	(85,000)	(85,000)	(85,000)	(85,000)	(85,000)	(85,000)	(85,000)	(52,308)
LH Treatment	115,581	Sep-20	Sep-21	0	0	0	0	0	115,581	115,581	115,581	115,581	115,581	115,581	115,581	115,581	115,581	71,127
Monitoring System	(7,500)	Sep-20	Sep-21	0	0	0	0	0	(7,500)	(7,500)	(7,500)	(7,500)	(7,500)	(7,500)	(7,500)	(7,500)	(7,500)	(4,815)
Golden Acres	145,828	Sep-20	Sep-21	0	0	0	0	0	145,828	145,828	145,828	145,828	145,828	145,828	145,828	145,828	145,828	89,740
Monitoring System	(15,000)	Sep-20	Sep-21	0	0	0	0	0	(15,000)	(15,000)	(15,000)	(15,000)	(15,000)	(15,000)	(15,000)	(15,000)	(15,000)	(9,231)
Great Oaks	95,516	Sep-20	Sep-21	0	0	0	0	0	95,516	95,516	95,516	95,516	95,516	95,516	95,516	95,516	95,516	58,700
Monitoring System	(10,000)	Sep-20	Sep-21	0	0	0	0	0	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(10,000)	(6,154)
River Bluffs	456,151	May-20	Sep-21	0	0	0	0	0	456,151	456,151	456,151	456,151	456,151	456,151	456,151	456,151	456,151	280,709
Over Budget	(305,832)	May-20	Sep-21	0	0	0	0	0	(305,832)	(305,832)	(305,832)	(305,832)	(305,832)	(305,832)	(305,832)	(305,832)	(305,832)	(188,081)
Monitoring System	(18,000)	May-20	Sep-21	0	0	0	0	0	(18,000)	(18,000)	(18,000)	(18,000)	(18,000)	(18,000)	(18,000)	(18,000)	(18,000)	(11,077)
Persimmon Ridge	175,167	Sep-20	Sep-21	0	0	0	0	0	175,167	175,167	175,167	175,167	175,167	175,167	175,167	175,167	175,167	107,795
Monitoring System	(40,000)	Sep-20	Sep-21	0	0	0	0	0	(40,000)	(40,000)	(40,000)	(40,000)	(40,000)	(40,000)	(40,000)	(40,000)	(40,000)	(24,615)
Timberland	252,169	Sep-20	Sep-21	0	0	0	0	0	252,169	252,169	252,169	252,169	252,169	252,169	252,169	252,169	252,169	155,181
Monitoring System	(8,000)	Sep-20	Sep-21	0	0	0	0	0	(8,000)	(8,000)	(8,000)	(8,000)	(8,000)	(8,000)	(8,000)	(8,000)	(8,000)	(4,923)
Arcadia Pines	30,938	Nov-20	Sep-21	0	0	0	0	0	30,938	30,938	30,938	30,938	30,938	30,938	30,938	30,938	30,938	19,039
Carriage Park	62,318	Nov-20	Sep-21	0	0	0	0	0	62,318	62,318	62,318	62,318	62,318	62,318	62,318	62,318	62,318	38,350
Marshall Ridge	44,516	Nov-20	Sep-21	0	0	0	0	0	44,516	44,516	44,516	44,516	44,516	44,516	44,516	44,516	44,516	27,395
Randview	178,424	Nov-20	Sep-21	0	0	0	0	0	178,424	178,424	178,424	178,424	178,424	178,424	178,424	178,424	178,424	109,799
Delaplain	857,793	Feb-21	Apr-22	0	0	0	0	0	0	0	0	0	0	0	0	0	0	857,793
Herrington Haven	160,450	Feb-21	Apr-22	0	0	0	0	0	0	0	0	0	0	0	0	0	0	160,450
SpringCrest	70,814	Feb-21	Apr-22	0	0	0	0	0	0	0	0	0	0	0	0	0	0	70,814
Woodland Acres	347,862	Mar-21	Apr-22	0	0	0	0	0	0	0	0	0	0	0	0	0	0	347,862
<b>Totals</b>	<b>\$ 3,583,650</b>			<b>\$ 256,388</b>	<b>\$ 256,388</b>	<b>\$ 256,388</b>	<b>\$ 256,388</b>	<b>\$ 256,388</b>	<b>\$ 2,146,731</b>	<b>\$ 2,146,731</b>	<b>\$ 1,530,210</b>							
Add: 2019 Constructions																		300,000
Less:																		
Randview																		(65,964)
Delaplain - Wastewater																		(12,342)
Herrington Haven - Wastewater																		(5,447)
SpringCrest - Wastewater																		(28,759)
Commission's 13-Month Average UPIS																		1,719,678
Less: B GW 13-Month Average UPIS																		(8,438,874)
UPIS Adjustment																		<b>\$ (6,719,196)</b>



13-Month Average UPIs - Water																	
System	Total Estimated Project Budget	Estimated Project															13-Month Average
		Start Date	End Date	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21	Jan-22	Feb-22	Mar-22	Apr-22	
Center Ridge WD01 - Water	\$ 152,910	Jun-20	Sep-21	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 152,910	\$ 152,910	\$ 152,910	\$ 152,910	\$ 152,910	\$ 152,910	\$ 152,910	\$ 152,910	\$ 94,098
Center Ridge WD02 - Water	\$ 203,999	Jun-20	Sep-21	0	0	0	0	0	203,999	203,999	203,999	203,999	203,999	203,999	203,999	203,999	125,538
Center Ridge WD03 - Water	\$ 243,354	Jun-20	Sep-21	0	0	0	0	0	243,354	243,354	243,354	243,354	243,354	243,354	243,354	243,354	149,756
Center Ridge WD04 - Water	\$ 137,046	Jun-20	Sep-21	0	0	0	0	0	137,046	137,046	137,046	137,046	137,046	137,046	137,046	137,046	84,336
Monitoring	\$ (40,000)	Jun-20	Sep-21						(40,000)	(40,000)	(40,000)	(40,000)	(40,000)	(40,000)	(40,000)	(40,000)	(24,615)
Eliminated Projects	\$ (15,000)	Jun-20	Sep-21						(15,000)	(15,000)	(15,000)	(15,000)	(15,000)	(15,000)	(15,000)	(15,000)	(9,231)
Totals				\$ -	\$ -	\$ -	\$ -	\$ -	\$ 682,310	\$ 682,310	\$ 682,310	\$ 682,310	\$ 682,310	\$ 682,310	\$ 682,310	\$ 682,310	419,882
Less: BGW 13-Month Average UPIs																	(1,188,537)
UPIs Adjustment																	\$ (768,655)

13-Month Average CWP - Water																					
	Estimated Project		Total		Beginning													13-Month Average			
	Start Date	End Date	Estimated Project Budget	Forecasted Year Construction	Base Year Construction	Suspension Construction	Beginning Forecasted Construction	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21	Jan-22		Feb-22	Mar-22	Apr-22
Center Ridge WD01 - Water	Jun-20	Sep-21	\$ 152,910	\$ 46,307	\$ 61,426	\$ 45,177	\$ 106,603	\$ 115,864	\$ 125,125	\$ 134,386	\$ 143,647	\$ 152,908	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 51,687
Center Ridge WD02 - Water	Jun-20	Sep-21	203,999	51,629	102,000	50,370	152,370	162,696	173,022	183,348	193,674	204,000	0	0	0	0	0	0	0	0	70,518
Center Ridge WD03 - Water	Jun-20	Sep-21	243,354	101,333	43,159	98,862	142,021	162,288	182,555	202,822	223,089	243,356	0	0	0	0	0	0	0	0	78,008
Center Ridge WD04 - Water	Jun-20	Sep-21	137,046	45,766	46,631	44,650	91,281	100,434	109,587	118,740	127,893	137,046	0	0	0	0	0	0	0	0	45,669
		Sep-21		(40,000)			(40,000)	(48,000)	(56,000)	(64,000)	(72,000)	(80,000)	0	0	0	0	0	0	0	0	(24,615)
		Sep-21		(15,000)			(15,000)	(18,000)	(21,000)	(24,000)	(27,000)	(30,000)	0	0	0	0	0	0	0	0	(9,231)
Totals			\$ 737,310	\$ 190,035	\$ 253,216	\$ 239,058	\$ 437,275	\$ 475,282	\$ 513,289	\$ 551,296	\$ 589,303	\$ 627,310	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	-
Commission's 13-Month Average CWP																					212,036
Less: BGW 13-Month Average CWP																					(97,909)
CWP Adjustment																					\$ 114,127

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 2020-00290 DATED AUG 02 2021

Water Rates

Center Ridge Water System

Flat Rate \$77.63 Per Month

Nonrecurring Charges

Tap Fee	\$350.00
Connection	0.00
Reconnection	0.00
Late Payment Penalty	0.00
Returned Check Charge	0.00

Sewer Rates

All Systems except Delaplain, Herrington  
Haven, Springcrest, and Woodland Acres

Residential	\$85.97	Per Month per unit
Multi-Family	64.48	Per Month per unit
Non-residential/Commercial	214.93	Per Month per unit
Residential Equivalent 12,000 gallons		

Nonrecurring Charges

Airview Estates	
Tap On Fee	\$0.00
Late Payment Penalty	0.00
Returned Check Fee	0.00
Termination of Service Charge	0.00
Reconnection of Service Charge	0.00

Arcadia Pines

Late Payment Penalty	\$0.00
Tap On Fee	500.00

Brocklyn Subdivision

Tap On Fee	\$0.00
Late Payment Penalty	0.00
Returned Check Fee	0.00

Termination of Service Charge	0.00
Reconnection of Service Charge	0.00
Carriage Park	
Late Payment Penalty	\$0.00
Tap On Fee	0.00
Fox Run Estates	
Tap On Fee	\$0.00
Late Payment Penalty	0.00
Returned Check Fee	0.00
Termination of Service Charge	0.00
Reconnection of Service Charge	0.00
Kingswood Development	
Tap On Fee	\$0.00
Lake Columbia Estates	
Late Payment Penalty	\$0.00
Tap On Fee	\$0.00
Longview and Homestead Subdivisions	
Tap On Fee	\$0.00
Marshall Ridge	
Late Payment Penalty	\$0.00
Tap On Fee	500.00
Great Oaks Subdivision	
Late Payment Penalty	\$0.00
Returned Check Fee	0.00
Field Collection Charge	0.00
Tap On Fee	750.00
Reconnection Fee	0.00
Golden Acres Subdivision	
Late Payment Penalty	\$0.00
Returned Check Fee	0.00
Field Collection Charge	0.00

Tap On Fee	250.00
Reconnection Fee	0.00
Persimmon Ridge Subdivision	
Late Penalty Payment	0.00
Tap On Fee	0.00
Randview	
Late Payment Penalty	\$0.00
Connection Fee	0.00
Reconnection Fee	0.00
Duplex	
Connection Fee	0.00
Reconnection Fee	0.00
Tap On Fee	0.00
City of River Bluffs & Environs	
Late Payment Penalty	\$0.00
Tap On Fee	0.00
Timberland Subdivision	
Late Payment Penalty	\$0.00
Tap On Fee	0.00

## APPENDIX C

### APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2020-00290 DATED AUG 02 2021

	Apr-20	May-20	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21
Bluegrass Water Connections	3,408	3,408	3,408	3,408	3,408	3,408	3,408	3,408	3,408	3,408	3,408	3,408	3,408
Total CSWR Connections	52,605	52,605	59,605	59,605	59,605	69,805	69,805	69,805	85,000	85,000	85,000	85,000	85,000
Monthly Allocation Percentage	6.48%	6.48%	5.72%	5.72%	5.72%	4.88%	4.88%	4.88%	4.01%	4.01%	4.01%	4.01%	4.01%
													13-Month Average Allocation Percentage
													4.98%
Base Connections	52,605	52,605	59,605	59,605	59,605	69,805	69,805	69,805	85,000	85,000	85,000	85,000	85,000
Continual Additional Connections	35,000	35,000	35,000	35,000	35,000	35,000	35,000	35,000	35,000	35,000	35,000	35,000	35,000
Total Connections	87,605	87,605	94,605	94,605	94,605	104,805	104,805	104,805	120,000	120,000	120,000	120,000	120,000
Percentage of Connections Attributed to BD per Month	39.95%	39.95%	37.00%	37.00%	37.00%	33.40%	33.40%	33.40%	29.17%	29.17%	29.17%	29.17%	29.17%
													13 Month Average
													33.61%

APPENDIX D

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 2020-00290 DATED AUG 02 2021

CSWR, LLC General & Administrative Budget

Admin & Human Resources	\$ 6,320,268	(236,282)		Adjustment to Forecast Number
		(691,141)		Removal of Unfilled Vacant Position Compensation
		(139,338)		Adjustment to Health Insurance
		(21,248)		Adjustment to Dental Insurance
		(177,289)		Allowance for 3% salary raise from the end of base period
		(102,000)		Removal of Executive Auto Allowance
		(8,864)	4,944,106	Adjustment to 401(k) Matching
Office Supplies	106,271		106,271	
Management Consulting	243,300	(243,300)		- Failure to Meet Burden
Engineering Consulting	20,400		20,400	
Auditor & Accounting Services	133,000		133,000	
Legal Fees	87,684		87,684	
IT	238,250		238,250	
Rent	168,000		168,000	
Insurance	77,000		77,000	
Miscellaneous	6,000		6,000	
<b>Total Corporate SG&amp;A</b>	<b>\$ 7,400,173</b>		<b>\$ 5,780,711</b>	

Total Adjusted Corporate SG&A	\$ 5,780,711
Multiply By: BD Percentage	<u>33.61%</u>

Allocated BD	<u><u>1,942,814</u></u>
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Total Adjusted Corporate SG&A	5,780,711
Subtract: Allocated BD	<u>1,942,814</u>

Allocatable Corporate SG&A	<u><u>\$ 3,837,897</u></u>
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Multiply by: Overhead Allocation Percentage	4.98%
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Bluegrass Water Allocated Overhead	\$ 191,127
KY Specific Travel Expense	<u>\$ 11,392</u>

Bluegrass Water Overhead	<u><u>\$ 202,519</u></u>
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	<u>Bluegrass Customers</u>	<u>Percent of Total Customers</u>	<u>Annual OHA</u>	
Sewer	2,321	87.35%	\$	176,909
Water	<u>336</u>	<u>12.65%</u>	<u>\$</u>	<u>25,610</u>
Total	2,657			

## APPENDIX E

### APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2020-00290 DATED AUG 02 2021

Detailed Income Statement - Sewer						
Description	Bluegrass Water's Forecasted Test Year	Commission Adjustments	System Removal	Commission Forecasted Test Year	Revenue Increase	Commission Test-Year at New Rates
<u>Operating Revenues</u>						
Revenues - Sewer Service	\$ 1,154,988	\$ -	\$ (246,822)	\$ 908,166	\$ 959,583	\$ 1,867,749
<u>Operating Expenses</u>						
Operation and Maintenance						
Sewer - Contract Operations	1,029,348	0	(219,973)	809,375	0	809,375
Sewer - Other Operations	310,377	0	(66,328)	244,049	0	244,049
Sewer - Maintenance	112,008	0	(23,936)	88,072	0	88,072
Customer Billing Expense	75,237	0	(16,078)	59,159	0	59,159
Uncollectible Accounts	8,662	0	(1,851)	6,811	7,197	14,008
Allocated Overhead	292,902	(115,993)	(37,806)	139,103	0	139,103
Administrative Services	41,122	(35,450)	(1,212)	4,460	0	4,460
Property Insurance	172,604	0	(36,886)	135,718	0	135,718
Regulatory Expense	6,322	0	(1,351)	4,971	0	4,971
PSC Assessment	841	975	0	1,816	1,919	3,735
Total Operation and Maint. Exp.	<u>2,049,424</u>	<u>(150,468)</u>	<u>(405,421)</u>	<u>1,493,535</u>	<u>9,116</u>	<u>1,502,651</u>
<u>Other Expenses</u>						
Depreciation - Net of CIAC Amort	264,095	(214,398)	0	49,697	0	49,697
State Income Tax	0	(28,544)	0	(28,544)	47,523	18,979
Federal Income Tax	0	(113,889)	0	(113,889)	189,618	75,729
General Taxes	17,622	0	(3,766)	13,856	0	13,856
Total Other Expense	<u>281,716</u>	<u>(356,831)</u>	<u>(3,766)</u>	<u>(78,880)</u>	<u>237,141</u>	<u>158,261</u>
Total Operating Expenses	<u>2,331,141</u>	<u>(507,299)</u>	<u>(409,187)</u>	<u>1,414,654</u>	<u>246,257</u>	<u>1,660,911</u>
Net Utility Operating Income	<u>\$ (1,176,153)</u>	<u>\$ 507,299</u>	<u>\$ 162,365</u>	<u>\$ (506,488)</u>	<u>\$ 713,326</u>	<u>\$ 206,838</u>

## APPENDIX F

### APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2020-00290 DATED AUG 02 2021

Detailed Income Statement - Water					
Description	Bluegrass Water's Forecasted Test Year	Commission Adjustments	Commission Forecasted Test Year	Revenue Increase	Commission Test-Year at New Rates
<u>Operating Revenues</u>					
Revenues - Water Sales	\$ 90,000	\$ -	\$ 90,000	\$ 223,001	\$ 313,001
<u>Operating Expenses</u>					
Operation and Maintenance:					
Water - Contract Operations	144,048	0	144,048	0	144,048
Water - Other Operations	30,000	0	30,000	0	30,000
Water - Maintenance	7,488	0	7,488	0	7,488
Customer Billing Expense	10,823	0	10,823	0	10,823
Uncollectible Accounts	675	0	675	1,673	2,348
Allocated Overhead	43,059	(17,449)	25,610	0	25,610
Administrative Services	7,109	(6,176)	933	0	933
Property Insurance	10,812	0	10,812	0	10,812
Regulatory Expense	0	180	180	446	626
Total Operating and Maint. Exp.	254,014	(23,445)	230,569	2,119	232,688
<u>Other Expenses</u>					
Depreciation - Net of CIAC Amort	31,941	(20,274)	11,667	0	11,667
<u>State Tax</u>					
State Income Tax	0	(6,275)	(6,275)	11,044	4,769
Current Federal Income Tax	0	(25,037)	(25,037)	44,066	19,029
General Taxes	92	0	92	0	92
Total Other Expense	32,033	(51,586)	(19,553)	55,110	35,557
Total Operating Expenses	286,047	(75,031)	211,016	57,229	268,245
Utility Operating Income	\$ (196,047)	\$ 75,031	\$ (121,016)	\$ 165,772	\$ 44,756

\*L Allyson Honaker  
Goss Samford, PLLC  
2365 Harrodsburg Road, Suite B325  
Lexington, KENTUCKY 40504

\*Bluegrass Water Utility Operating Company, LLC  
1650 Des Peres Road, Suite 300  
St. Louis, MO 63131

\*Angela M Goad  
Assistant Attorney General  
Office of the Attorney General Office of Rate  
700 Capitol Avenue  
Suite 20  
Frankfort, KENTUCKY 40601-8204

\*J. Michael West  
Office of the Attorney General Office of Rate  
700 Capitol Avenue  
Suite 20  
Frankfort, KENTUCKY 40601-8204

\*David S Samford  
Goss Samford, PLLC  
2365 Harrodsburg Road, Suite B325  
Lexington, KENTUCKY 40504

\*John G Horne, II  
Office of the Attorney General Office of Rate  
700 Capitol Avenue  
Suite 20  
Frankfort, KENTUCKY 40601-8204

\*Kathryn A Eckert  
McBrayer PLLC  
201 East Main Street  
Suite 900  
Lexington, KENTUCKY 40507

\*Katherine Yunker  
McBrayer PLLC  
201 East Main Street  
Suite 900  
Lexington, KENTUCKY 40507

\*Larry Cook  
Assistant Attorney General  
Office of the Attorney General Office of Rate  
700 Capitol Avenue  
Suite 20  
Frankfort, KENTUCKY 40601-8204