

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF KENTUCKY-AMERICAN WATER) CASE NO.
COMPANY TO INCREASE ITS RATES) 95-554

O R D E R

On October 4, 1996, the Kentucky-American Water Company ("Kentucky-American") filed a petition requesting the Commission to rehear three issues adjudicated in the September 11, 1996 rate Order. Those issues are: 1) The exclusion from rate base of the billing and tariff group ("BAT Group") costs which include the cost of the cost-of-service study; 2) the exclusion from rate base of the automated meter reading study ("AMR Study") costs; and 3) the effective date of the new rates. The Attorney General's Office of Rate Intervention ("AG") also requested rehearing on the following five issues: 1) The inclusion in rate base of the cost to paint Kentucky-American's logo on the water tanks; 2) the inclusion in rate base of the web site development cost; 3) additional revenues from the Lexington-Fayette Urban County Government; 4) above the line treatment of spousal travel; and 5) the percentage increase in Kentucky-American's customer charge. The Commission's finding on each of these issues is set forth below.

BAT Group Costs. Kentucky-American asserts that when the Commission reduced rate base by \$97,144 to eliminate the BAT Group costs, it inadvertently eliminated the costs associated with its cost-of-service study. Kentucky-American pointed to the Commission's past practice of allowing the unamortized cost-of-service

study expenses in rate base. Therefore, Kentucky-American requested that rate base be increased by \$22,364, the unamortized cost of its cost-of-service study net of deferred income taxes.

In its Order, the Commission pointed to the BAT Group's monthly billing recommendation and how it benefited the stockholders by decreasing the time lag between the provision of water service and receipt of the payment. Kentucky-American argues that monthly billing will provide a greater benefit to its ratepayers because it will reduce uncollectible expense, decrease hidden leaks, and increase cash flow. Kentucky-American encouraged the dialogue to implement monthly billing and collection, because of the Commission's perceived endorsement of the concept of monthly billing in Case No. 94-197. For these reasons Kentucky-American requested that the unamortized cost of the BAT Group be included in rate base.

Kentucky-American's Workpaper W/P-1-12, Calculation of Average Rate Base Elements Deferred Debits, did not separate the unamortized BAT Group costs from the cost of service. Consequently, the Commission was not aware that the cost-of-service study was included with the BAT Group costs. The Commission has traditionally included the unamortized cost of the cost-of-service study in rate base since such a study does not directly benefit the stockholders. Therefore, rehearing will be granted including the unamortized cost of the cost-of-service study in rate base.

Kentucky-American did not dispute the Commission's finding that the BAT Group benefited both the ratepayers and stockholders. Kentucky-American has presented no

argument or cited any evidence to persuade the Commission to grant rehearing on the other BAT Group costs.

AMR Study Costs. Because Kentucky-American's ratepayers are not currently receiving a benefit from the AMR Study and there is no certainty that the automated meter reading program will be implemented, the Commission excluded the unamortized cost of the AMR Study from rate base.

Kentucky-American pointed to the fact that the AMR Study was performed in direct response to a recommendation in the Schumaker & Company management audit. Further, Kentucky-American argues that the study was necessary to determine the costs and benefits of automated meter reading. Although the study concluded that the cost outweighs the benefit, Kentucky-American claims that its ratepayers benefited by the determination that automated meter reading not be implemented at this time. Since the Commission has traditionally included in rate base unamortized costs incurred to benefit the ratepayers, rehearing will be granted on this issue.

Effective Date of the Rates. Kentucky-American argues that the rates approved in the September 11, 1996 Order should be effective for service rendered on and after August 29, 1996, rather than from the date of the Order. Kentucky-American proposed to recover the claimed lost revenue of \$53,958 through a surcharge.

The Commission had suspended Kentucky-American's proposed rates through August 28, 1996. When no rate order was issued by that date, Kentucky-American, served notices, pursuant to KRS 278.190 (2), of its intent to place the proposed rates into effect on August 29, 1996. However, to avoid the expense of placing the proposed

rates into effect, having to make refunds and revising the rates on its computer, Kentucky-American chose to delay billing for meters read from August 29, 1996 through September 11, 1996, the date the rate order was issued.

Kentucky-American argues that having placed its proposed rates into effect on August 29, 1996, the new rates subsequently approved by the Commission should have an effective date of August 29, 1996. While the Commission traditionally makes new rates effective as of the end of the suspension period when the utility has already placed the proposed rates into effect, there is a factual issue here of whether the proposed rates were placed into effect. Therefore, the Commission will grant rehearing on this issue.

Logo Costs. The Commission's Order inadvertently omitted a specific finding on the AG's proposed adjustment to remove the cost of painting Kentucky-American's logo and striping on four water towers. The AG claims that the logos are a promotional amenity and allowing recovery of this cost permits Kentucky-American to do indirectly what it may not do directly.

Placing the company name or logo on the side of a water tank is the standard practice of the water industry. It is common for not-for-profit water districts and associations that do not engage in promotional advertising to paint the utility name on their water towers. The Commission agrees with Kentucky-American's position that its logo communicates to the community the facility owner and is similar to the practice of all utilities in displaying a sign outside their offices, placing a logo on their vehicles, or painting the logo on their facilities. These were the reasons why the cost of painting the

logos was not removed. This is a legitimate utility expense and other than to reflect this finding no rehearing should be granted.

Web Site Development Cost. The Commission's Order also inadvertently omitted a specific finding on the AG's proposed adjustment to remove the cost to develop the Web site from rate base. The AG claims that any ratepayer benefit is wholly speculative. Therefore, this issue goes directly to the question of how to allocate costs between the ratepayers and shareholders.

The record evidence demonstrates that Kentucky-American's Web site will give the ratepayers 24-hour, 7 day a week access to account history and billing information; information on how to read a water meter; allow for the set-up of automatic payment plans; and the date of the next scheduled meter reading. Furthermore, the Web site development costs cited by the AG include the cost of an Internet station that will be used by Kentucky-American employees to access information related to water quality studies, environmental standards, AWWA library and Human Resource information.

The September 11, 1996 Order should have included the finding that ratepayers will receive benefits from this cost and therefore rehearing on this issue is denied.

Revenues from LFUCG. The AG maintains that the Commission should impute a reasonable estimate of the additional revenue to be received from LFUCG associated with the conversion from quarterly to monthly billing. In the alternative, the AG suggests that the Commission mandate that any additional revenues be accumulated in a deferred credit or require Kentucky-American to file an application for a reduction in rates based on any additional revenues associated with the execution of a new agreement.

The September 11, 1996 Order stated that Kentucky-American is currently negotiating with LFUCG regarding additional revenues from monthly billing of sewer services. The Commission concluded that while LFUCG should pay an appropriate share of the monthly billing costs, no contract has been signed and any adjustment to revenue would be speculative, and thus cannot be made at this time. Furthermore, the speculative nature of such a revenue adjustment will not justify imputing additional revenues. The Commission also finds that since Kentucky-American typically files a rate case every 15-18 months, there is no need to establish a deferred credit account or require the filing of a single issue rate case, even assuming that the latter is justified for an item of this magnitude.

Spousal Travel. The Commission disallowed several miscellaneous expenses from forecasted operations based on findings that they had been excluded as inappropriate in prior cases and Kentucky-American had failed to provide any new evidence to now justify their inclusion. The AG argues that in Case No. 92-452, the Commission determined the cost of spousal travel to be inappropriate and denied above-the-line treatment for the cost. Based on this past precedent, the AG requests that spousal travel of \$762 be eliminated from forecasted operations.

The Commission agrees with the AG's position. Spousal travel has historically been excluded from rates but was inadvertently included in this case. Therefore, the Commission will grant rehearing on this issue.

Customer Charge. Once the amount of the revenue deficiency is determined, there are two generally accepted methodologies for increasing rates: either the revenue

deficiency is spread across the board on an equal percentage basis, which would have resulted in all customers receiving a 4.59 percent increase in this case; or a cost-of-service study is performed to allocate the expenses to serve each customer class consistently with the cost to serve that class.

The AG argues that the customer charge should be reduced because its increase, from \$5.85 to \$6.62, was 13 percent, while the overall rate increase granted was approximately 4.59 percent. In its response, Kentucky-American maintains that the purpose of preparing a cost-of-service study is to determine whether costs have changed and, if they have, rates should be adjusted.

One reason the customer charge increased by 13 percent is that the costs to convert to monthly meter reading and billing are fully allocated to the customer charge. While a residential customer who uses no water and pays only the customer charge will experience a 13 percent increase, the typical customers using a monthly average of 6,000 gallons will experience a 6.0 percent increase.

The Commission finds that an increase in the customer charge of 13 percent does not justify deviating from the cost-of-service study. Therefore, rehearing on this issue is denied.

IT IS THEREFORE ORDERED that:


1. Rehearing is granted on the issues of: 1) excluding the cost of the cost-of-service study from rate base; 2) excluding the AMR Study costs from rate base; 3) the effective date of the new rates; and 4) the rate-making treatment of spousal travel expenses.

2. Rehearing is denied on all other issues.
3. The September 11, 1996 Order is modified to reflect the findings herein on the issues of logo cost and Web site development cost.
4. The procedural schedule attached hereto in Appendix A shall be followed.

Done at Frankfort, Kentucky, this 18th day of October, 1996.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman

Commissioner

ATTEST:



Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 95-554 DATED October 18, 1996.

Kentucky-American's prefiled testimony shall be due no later than.....	11/08/96
All requests for information to Kentucky-American shall be due no later than.....	11/19/96
Kentucky-American shall mail or deliver responses to the requests for information no later than.....	12/02/96
Intervenor testimony, if any, shall be filed in verified prepared form no later than.....	12/16/96
All requests for information to Intervenors shall be due no later than.....	12/23/96
Intervenors shall mail or deliver responses to requests for information no later than.....	01/06/97
Public Hearing is to begin at 10:00 a.m., Eastern Standard Time, in Hearing Room 1 of the Commission's offices at 730 Schenkel Lane, Frankfort, Kentucky, for the purpose of cross-examination of witnesses of Kentucky-American and witnesses of the Intervenors.....	To be scheduled