

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

IN THE MATTER OF:

**ADJUSTMENT OF THE RATES OF
KENTUCKY-AMERICAN WATER COMPANY)**

CASE NO. 2004-00103

**REBUTTAL TESTIMONY
OF
COLEMAN D. BUSH
ON BEHALF OF
KENTUCKY-AMERICAN WATER COMPANY**

October 8, 2004

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2004-00103
Rebuttal Testimony
Coleman D. Bush

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1. Q. PLEASE STATE YOUR NAME FOR THE RECORD.

A. My name is Coleman D. Bush.

2. Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my rebuttal testimony is to address certain comments and recommendations made by the Attorney General's witnesses, Ms. Crane and Mr. Rubin.

3. Q. WHAT ARE THE ISSUES THAT YOU WILL BE ADDRESSING IN YOUR REBUTTAL TESTIMONY?

- A. I will be addressing these issues:
- Adjustment proposed by Ms. Crane to deny rate treatment for utility plant acquisition adjustments for Tri-Village and Elk Lake Systems – pages 13-18 of Direct Testimony of Andrea C. Crane
 - Adjustment proposed by Ms. Crane to eliminate three employee positions included in the Company's revenue requirement – pages 48-50 of Direct Testimony of Andrea C. Crane
 - Adjustment proposed by Ms. Crane to eliminate social club dues from the Company's revenue requirement – page 67 of Direct Testimony of Andrea C. Crane
 - Adjustment proposed by Ms. Crane to eliminate certain advertising costs – pages 68-69 of Direct Testimony of Andrea C. Crane
 - Comments and recommendation made by Mr. Rubin regarding the Company's proposed Emergency Pricing Tariff – pages 4-9 of Direct Testimony of Scott J. Rubin
 - Comments and recommendation made by Mr. Rubin regarding the Company's proposed Activation Fee – pages 11-13 of Direct Testimony of Scott J. Rubin

1 **Utility Plant Acquisition Adjustment**

2
3 **4. Q. WHAT IS MS. CRANE'S RECOMMENDATION REGARDING THE UTILITY**
4 **PLANT ACQUISITION ADJUSTMENTS FOR THE TRI-VILLAGE AND ELK**
5 **LAKE SYSTEMS INCLUDED BY THE COMPANY IN ITS FILING?**

6 **A.** Ms. Crane recommends that these acquisition adjustments be denied. I disagree
7 with this recommendation.
8

9 **5. Q. WHY DO YOU DISAGREE WITH MS. CRANE'S RECOMMENDATION TO**
10 **DENY THE UTILITY PLANT ACQUISITION ADJUSTMENTS FOR THE TRI-**
11 **VILLAGE AND ELK LAKE SYSTEMS?**

12 **A.** Ms. Crane makes a great deal of the issue that the Company viewed the
13 acquisitions of Tri-Village and Elk Lake as business development opportunities.
14 One page 69 of her Direct Testimony, she ascribes the adjective "oxymoronic" to
15 the business development activities of a regulated water utility. In fact, Kentucky
16 American Water is a business. Even municipal water utilities should be run as
17 businesses by observing best practices in their operations and by asking their
18 customers to bear the full and reasonable costs of service. I guess I have to ask,
19 "What is wrong with business and what is wrong with developing business?"
20

21 The Commonwealth of Kentucky has encouraged regionalization of water
22 suppliers and the merger of smaller and less efficient water systems and the
23 Commission has supported the undertaking of related projects in cases where the
24 Delta Natural Gas Co. criteria are met. Such regionalization cannot be
25 accomplished without business development. The real issue at hand is whether
26 these acquisitions meet the Delta Natural Gas Co. criteria. The Company
27 addressed each criterion in its response to PSCDR2#82 and feels that it has met
28 the burden of proof, but it is important to elaborate here on the most basic, but
29 most important criterion – the purchase will result in overall benefits in service
30 aspects of a utility's operation and will therefore, in one form or another provide
31 benefits in the financial aspects of a utility's operation. The criterion that the
32 purchase **will** result in overall benefits in the financial and service aspects of the
33 utility's operations indicates that these benefits do not have to inure immediately.

1 In the case of the Tri-Village system, before Kentucky American Water purchased
2 the system, Tri-Village was routinely required by state regulators to provide public
3 notice to its customers that its water exceeded health limits for disinfection by-
4 products. Because of the water quality expertise of the Company and its
5 application to the Tri-Village system, there have been no occurrences of public
6 notification due to exceeding health limits for disinfection by-products since and
7 even before Kentucky American purchased the system. In the case of the Elk
8 Lake system, the Elk Lake system water treatment plant was inadequate to meet
9 the filtered turbidity limits that will go into effect January 1, 2005. Consolidation of
10 the Elk Lake system into a larger system seems to be exactly what the
11 Commonwealth had in mind with Senate Bill 409 (KRS 224A.300). I cannot really
12 say what the Tri-Village system would have spent to combat its disinfection by-
13 product problem or if they ever would have solved it without the expertise
14 provided by the country's largest water utility. They might have resorted to an
15 expensive capital improvement solution when, in this case, water treatment
16 expertise provided the much needed solution. I also do not believe it would have
17 been the correct decision for the Elk Lake system to build a new treatment plant,
18 on what some would consider a water source inadequate in both quantity and
19 quality, to serve approximately 300 customers. Some benefits may be delayed
20 but as the water business is a long term business, that fact does not make the
21 wisdom of those decisions any less. Mr. Miller has offered in his testimony and in
22 response to requests for information the benefits that accrue to the current
23 customers of Kentucky American Water as a result of such transactions. In my
24 opinion, both acquisitions meet the Delta Natural Gas Co. criteria and the
25 associated acquisition adjustments should be afforded the requested treatment in
26 rates.

27
28 **Elimination of Three Employee Positions**

29
30 **6. Q. MS. CRANE IS RECOMMENDING THAT COSTS FOR THREE EMPLOYEE**
31 **POSITIONS BE ELIMINATED FROM THE COMPANY'S REVENUE**
32 **REQUIREMENT CLAIM, IN RECOGNITION OF EMPLOYEE VACANCIES. CAN**
33 **YOU OFFER SUPPORT TO COUNTER THIS RECOMMENDATION?**

1 A. The Company's labor claim does include 133 full-time equivalent employees.
2 The forecast for labor does include a forecast for overtime hours based on
3 "actual levels experienced in the past with adjustments made based on
4 judgment and forecasted operational needs." These adjustments, based on
5 judgment and forecasted operational needs, include a reduction in forecasted
6 overtime hours, which is reflective of forecasting a full complement of
7 employees. For example, the forecast in this case includes 14,899 overtime
8 hours. Our actual experience, as of the end of September 2004, is 16,306.50
9 overtime hours or if annualized, 21,740 hours. We incurred 19,532.75 actual
10 overtime hours in 2003. Regardless of the number of employee vacancies that
11 the Company has at any one time, the level of work required to be done does
12 not necessarily decrease. Average overtime hours for 2004 (annualized) and
13 2003 are 20,636. This is 5,737 hours more than included in the forecast. At 1.5
14 times, this is equivalent to 8,605 hours, which is equal to four additional
15 employees. The Company also compensates for employee vacancies by using
16 temporary labor. Through the first nine months of this year, the Company has
17 incurred \$120,060 in temporary labor expense yet we have only \$90,872
18 included in contract services – temporary labor in the forecast. Our forecast for
19 temporary labor is less than actually experienced in the recent past in
20 recognition of the fact that we have budgeted a full complement of employees.
21 In summary, the inclusion of 133 full-time equivalent positions is appropriate
22 and Ms. Crane's recommendation to eliminate three employee positions is not
23 appropriate. She provides no basis for a reduction in the work to be performed
24 and accordingly, there is no basis to reduce the expense that the Company
25 must incur to perform the work it has ahead of it, whatever form that expense
26 might take. The onus is on the Company to fill employee vacancies as soon as
27 possible. It has been demonstrated that the inefficiencies created by incurring
28 excessive overtime and hiring temporary labor, will, in the long run, cause the
29 Company to incur additional expenses, expenses that we are not requesting in
30 this case.

31
32 **Social Club Dues**

1 **7. Q. MS. CRANE INCLUDES AN ADJUSTMENT IN HER DIRECT TESTIMONY IN**
2 **SCHEDULE ACC-32, WHICH PROPOSES THE ELIMINATION OF \$5,228 FOR**
3 **SOCIAL CLUB DUES FROM THE COMPANY'S REVENUE REQUIREMENT?**
4 **DO YOU AGREE WITH THIS ADJUSTMENT?**

5 A. Schedule F-1 of Exhibit 37 of the filing documents actually speaks to Social
6 Organization/Service Club expenses and not just social club dues. Schedule F-1
7 shows that expenses for Spindletop Hall and Keeneland Club, both social
8 organizations, are included in accounts 426.41 and 426.42, which are below-the-
9 line expenses and are appropriately excluded from the Company's revenue
10 requirement in the Company's filing. The memberships in the Lafayette Club
11 and the U.K. Faculty Club are for business purposes only. The Company uses
12 these facilities for business luncheons or for business meetings. Both facilities
13 have private rooms where off-site business meetings, seminars, training
14 sessions, etc. can be conducted. Rotary and Kiwanis Clubs are well known
15 service organizations. I feel the minor expense for these memberships is money
16 very well spent for the Company and the ratepayers and is appropriately included
17 in the Company's revenue requirement. In addition to an opportunity to share
18 with other business leaders in service to the community, participation in these
19 clubs, through interaction with other community leaders, offers valuable insight
20 into community events and trends, which insight is translated into better water
21 service to our customers. Our membership in the Audubon Society (\$90) is an
22 extension of the Company's commitment to conservation and the environment.

23
24 **Advertising Costs**

25
26 **8. Q. MS. CRANE RECOMMENDS THE DISALLOWANCE OF \$72,415 IN**
27 **INSTITUTIONAL ADVERTISING? DO YOU AGREE WITH THIS**
28 **RECOMMENDATION?**

29 A. No. Schedule F-4, from which Ms. Crane derives the amounts to be excluded,
30 was incorrectly prepared by the Company. The actual amount included in the
31 forecast for advertising is \$134,704 and can be found on W/P-3-13, page 1 of 7.
32 Exhibit KAW_RT_CDB_EX1_100804.pdf, which is attached to my rebuttal
33 testimony, provides the details of the Company's forecasted advertising expense.

1 While the Company regrets its error, the specific language referenced by Ms.
2 Crane is from past ads, which the Company included in response to
3 LFCDR1#45. As stated in its response to LFCDR1#45, the Company does not
4 believe that these past ads referenced by Ms. Crane constitute institutional
5 advertising and it does not believe that it has included any expenses for
6 institutional advertising in its forecasted revenue requirement. Again, the
7 Company apologizes for its error in the preparation of Schedule F-4, but believes
8 that its forecast included in this case contains only advertising expense eligible
9 for rate recovery.

10
11 **Emergency Pricing Tariff**

12
13 **9. Q. MR. RUBIN, THE ATTORNEY GENERAL'S WITNESS, STATES THAT, "IT**
14 **DOES NOT APPEAR THAT THE COMPANY HAS FULLY THOUGHT**
15 **THROUGH THE VERY COMPLEX IMPLEMENTATION AND PUBLIC POLICY**
16 **ISSUES PRESENTED BY ITS PROPOSAL." DO YOU AGREE WITH THAT**
17 **STATEMENT?**

18 **A.** No, but I am unable to summarize my thoughts in one sentence. That comment
19 from the Attorney General surprises me since his staff, specifically including Mr.
20 David Spenard and Mr. Dennis Howard, was involved in the development of this
21 tariff during its early stages. After the collaborative beginning to the tariff design,
22 it is disappointing that we did not get more meaningful input from the Attorney
23 General during this proceeding rather than his coming down from the hills after
24 the battle is over to simply shoot the wounded.

25
26 To say that this proposal is not well thought out is inaccurate in view of the
27 significant input into the development of the tariff by regulators and customers.
28 This proposal has been very well thought out as an additional measure, to be
29 taken during a drought emergency, to further restrict customer demand after all
30 non-essential water use has been eliminated. As stated in my Direct Testimony,
31 numerous meetings were held to give interested and affected parties an
32 opportunity to provide input on which to develop a foundation for this proposal:
33

1 "Meetings were held at the Commission offices on August 26, 1999; September 3,
2 1999 and September 17, 1999 including, at times, members of the Commission
3 staff, Mr. David Spenard and Mr. Dennis Howard of the Office of the Attorney
4 General and representatives from the Lexington-Fayette Urban County
5 Government. In addition, Kentucky American Water also conducted meetings at
6 its office on September 2, 1999; October 14, 1999 and June 16, 2000, which
7 included, at times, representatives from the GE Kentucky Glass Plant, Central
8 Kentucky Processing, Jessamine South Elkhorn Water District, LexMark,
9 Aramark, Spears Water Company (now owned by the city of Nicholasville),
10 University of Kentucky, Eastern State Hospital, Trane Company, Georgetown
11 Municipal Water And Sewer Service, Bluegrass Station Division, Square D, the
12 City of Midway, Toyota, Community Action Council and the then Lexington
13 Chamber of Commerce."

14
15 In addition, dozens of internal meetings and work sessions were conducted to
16 take this input along with input gleaned from other sources and fashion what I
17 consider to be a sound, but realistically a "draft" proposal. Just as this rate case
18 itself is a draft in that it will not survive the public process in its original form, this
19 proposal for an Emergency Pricing Tariff was not realistically expected to remain
20 untouched as I pointed out in my Direct Testimony. As I said, "While a great deal
21 of public input has been sought and given in the development of the Emergency
22 Pricing Tariff, we are proposing this tariff with the belief that it has been
23 developed in the spirit of fairness and equity for all customers, but also with the
24 realistic viewpoint that says it will not survive in its present form under the
25 necessary public scrutiny that will be part of this case."

26
27 As Mr. Rubin aptly points out concerning his appointment to an American Water
28 Works Association Research Foundation advisory committee tasked with the
29 responsibility to evaluate the effectiveness of water budget programs, water
30 budget programs, including their use as a drought response measure, raise many
31 complex issues. A person of his experience should also know that
32 notwithstanding all of the hard work and research that his committee will become
33 engaged in, the committee must eventually publish the study for public
34 consumption. The difference between his committee's study and the Emergency

1 Pricing Tariff is that the Emergency Pricing Tariff must pass legal muster and his
2 study has no such requirement. However, he is also experienced enough to know
3 that in spite of the research, drafting and redrafting that his committee will do on
4 this study, if a higher authority had a responsibility to approve the study before it
5 could be made public, it would never survive in the form submitted.

6
7 I agree with Mr. Rubin that this proposal is fraught with very complex
8 implementation and public policy issues, but that is no reason to reject a sound
9 and vital proposal – one that will be crucial to ensure public health and safety in
10 the event of a drought emergency.

11
12 There are no perfect laws, rules, procedures, or instruction manuals written by
13 humans and they even become less perfect in the event that they have to be
14 applied and used. What is closer to perfect is our ability as humans to be flexible
15 and to adapt to changing situations. In fact, based on input from our software
16 programmers, I am submitting a revised Emergency Pricing Tariff with this
17 testimony to reflect some of their suggestions. See attached exhibits
18 KAW_RT_CDB_EX2_100804.pdf and KAW_RT_CDB_EX2redline_100804.pdf.
19 This has been submitted in both final form and redline form for ease of
20 comparison.

21
22 If the Emergency Pricing Tariff, with any appropriate changes, is approved, and if
23 we ever have the extreme misfortune to experience a drought in this community
24 severe enough to cause us to enter the Rationing Phase of the Company's
25 Demand Management Plan, while none of us can see the exact issues, it is
26 almost a law of nature that issues will arise, which were never foreseen. And if
27 that happens and because successful utilization of the Emergency Pricing Tariff
28 at that time would be crucial to the health and safety of our community, we and
29 the Emergency Pricing Tariff will adapt to fit those unforeseen circumstances.

30
31 **10. Q. DOES THE COMPANY CURRENTLY HAVE THE BILLING SYSTEM IN PLACE**
32 **TO IMPLEMENT THE EMERGENCY PRICING TARIFF?**

33 **A.** Yes. However, modification of that system is necessary in order to implement
34 the Emergency Pricing Tariff. Our programmers, through Alliance Data Systems,

1 have the Custom Modification Document ("CMD") written and have provided us
2 with an estimate of the programming costs. Mr. Rubin is certainly correct in one
3 regard – there will be costs for computer programming. Alliance Data Systems
4 estimates that it will take 1,001 hours of programming in addition to the hours
5 already incurred to write the CMD. This does not include the option for interim
6 meter reading, which could require an additional 73-103 hours of programming.
7 Alliance Data Systems charges \$150 per hour for programming services. We will
8 not pursue the programming effort until we have a final non-appealable order
9 from the Commission.

10
11 **11. Q. MR. RUBIN POINTS OUT IN HIS TESTIMONY THAT DESPITE THE**
12 **COMPANY'S RESPONSE TO AGDR1#25 IT IS NOT THE INTENT OF THE**
13 **WATER CONSERVATION APPEALS BOARD TO ADDRESS ANY**
14 **GRIEVANCES ARISING FROM THE IMPLEMENTATION OF THE**
15 **EMERGENCY PRICING TARIFF. IS HE CORRECT ON THIS POINT?**

16 A. From my reading of the ordinance, he is correct on that point and I should have
17 realized that when I wrote the response since the Public Service Commission, in
18 this case, is the legal entity responsible for regulating utility rates and service. At
19 the time I prepared my response to AGDR1#25 I was aware of the existence of
20 the Water Conservation Appeals Board and its successful handling of the issues
21 that arose during the drought of 1999. However, while I can't speak for the
22 Commission, I see no reason that the Commission cannot grant Kentucky
23 American Water the power to use facts and judgment to settle grievances as
24 long as all customers are given the same opportunities or that the Public Service
25 Commission could not itself establish an Emergency Pricing Tariff Appeals Board
26 or even handle complaints regarding utility rates and service through its standard
27 processes. It appears to me that the Water Conservation Appeals Board
28 established by the Lexington-Fayette Urban County Government under
29 Ordinance 221-2000 could serve as a model for an appeals board.

30
31 **12. Q. MR. RUBIN ARGUES THAT THE "WATER BUDGET" IS NOT A TESTED**
32 **TOOL FOR DECREASING WATER DEMAND DURING AN EMERGENCY. DO**
33 **YOU AGREE THAT THE EMERGENCY PRICING TARIFF MIGHT NOT BE A**

1 **USEFUL TOOL IN RESTRICTING DEMAND DURING AND EMERGENCY AND**
2 **HAVE HIS ARGUMENTS CAUSED YOU TO CONSIDER WITHDRAWING THE**
3 **EMERGENCY PRICING TARIFF FROM CONSIDERATION IN THIS CASE?**

4 A. To the contrary, his comments have given me ideas on how to better implement
5 the tariff. If this tariff is ever implemented, it will be during an emergency, the like
6 of which has only been experienced once in this community and that was in
7 1930. This will certainly not be an ordinary time and any reasonable means to
8 preserve the health and safety of this community seems prudent to me. The
9 very fact that there are enough “water budgets” in place to give rise to a
10 committee to study them indicates that water budgets are perceived by
11 reasonable people as reasonable means to solve problems.

12
13 To be effective, the Company’s Demand management plan needs more than
14 one governor on its pipes. The threat of a fine proved effective during the
15 drought of 1999, but over 1,000 citations were issued in that year in spite of that
16 threat. Economic pricing, an example of which is included in the sample water
17 shortage plan developed by the Natural Resources and Environmental
18 Protections Cabinet’s Division of Water and the Public Service Commission, will
19 be the last line of defense. I am also attaching for reference exhibit
20 KAW_RT_CDB_EX3_100804.pdf, which is a copy of the Pennsylvania
21 Department of Environmental Protection’s *Guidelines for the Development of a*
22 *Local Water Rationing Plan*, September 25, 1995 edition. Section 13 addresses
23 Excess Use Charges.

24
25 **13. Q. MR. RUBIN’S TESTIMONY SUGGESTS THAT ONLY LOCAL GOVERNMENT**
26 **IS NIMBLE ENOUGH TO IMPLEMENT AND MANAGE AN EMERGENCY**
27 **PRICING TARIFF. DO YOU AGREEMENT WITH HIS ASSESSMENT?**

28 A. To suggest that only local government can implement and manage the
29 Emergency Pricing Tariff is not understandable. The lack of accountability by
30 local government that Mr. Rubin cites is perhaps one of the best reasons that
31 administration of this tariff belongs in the hands of Kentucky American Water and
32 the Public Service Commission. This local government cannot possibly deal with
33 a water shortage emergency better than the country’s largest water utility and the

1 Kentucky Public Service Commission. The Commission's own design for a water
2 shortage plan includes emergency pricing as a method to curtail demand. All
3 water utilities under the jurisdiction of the Public Service Commission were urged
4 by the Commission to develop a water shortage plan and to file that plan with the
5 Commission using the sample plan, which includes economic pricing as a
6 curtailment incentive, as the base for those plans. In Mr. Rubin's home state,
7 through the Pennsylvania Department of Environmental Protection's *Guidelines*
8 *for the Development of a Local Water Rationing Plan*, a plan is outlined for all
9 water purveyors ("the owner or operator of any public water supply system
10 including, but not limited to, any public utility, municipality, municipal authority,
11 association or other organization which supplies water to the public") to apply
12 excess use charges as part of a Local Water Rationing Plan needed to deal with
13 local water shortages caused by drought conditions.

14
15 **Activation Fee**

16
17 **14. Q. IN HIS TESTIMONY, MR. RUBIN RECOMMENDS THAT THE COMMISSION**
18 **DENY THE COMPANY'S REQUEST FOR AN ACTIVATION FEE. DO YOU**
19 **HAVE ANY ADDITIONAL INFORMATION TO PRESENT IN SUPPORT OF THE**
20 **ACTIVATION FEE?**

21 **A.** Yes. Our search has been far from exhaustive, but it is not difficult to find
22 examples where activation fees are in use or to find utility managers who
23 express an interest in them after we ask whether they have such a fee.

24
25 **Internal:**

26 From Pennsylvania American Water regarding its activation fee: "The fee was
27 calculated by having the Business Manager in our Mechanicsburg office review
28 the steps necessary when adding a customer. He took the average time it took
29 a customer service rep in his office to take the phone call and set up the account
30 in the customer accounting database. He also looked at the average time it took
31 a service person to drive to the midpoint of the service territory. He then
32 calculated the labor and transportation cost associated with these activities and
33 came up with \$30. I do not have a copy of his actual calculation and do not

1 remember if the calculation was supplied to the PUC years ago (my gut reaction
2 is yes, but the actual document had been taken offsite and probably destroyed).”

3
4 From our Central Region (Missouri, Illinois, Indiana, Iowa, Michigan and Ohio)
5 regarding activation fees: “The Central Region has a fee for Missouri and Iowa.
6 We cannot locate the workpapers that supported the calculation of the fees since
7 they are pretty old tariffs. But through some verbal discussions with individuals
8 regarding the development of the fees, it was determined that the fees were cost
9 based. Calculation of the fees was based on the average time for service clerks
10 and on/off people to perform an activation – labor costs, transportation, forms,
11 postage, return on assets employed and other miscellaneous overheads.”

12
13 Later, we did locate the workpaper for the Iowa American Water calculation and
14 that is attached as exhibit KAW_RT_CDB_EX4_100804.pdf.

15
16 Western Region (Arizona, California, Hawaii and New Mexico): A copy of a tariff
17 including an activation fee not filed in a response to previous data requests is
18 attached as exhibit KAW_RT_CDB_EX5_100804.pdf.

19
20 **External:**

21 The city of Lancaster, KY has a \$30 activation fee on all service changes.

22
23 East Clark County Water District (“ECCWD”) – see attached exhibit
24 KAW_RT_CDB_EX6_100804.pdf to view the notice published in The Winchester
25 Sun on September 25, 2004 to notice its customers regarding various fees
26 proposed by the ECCWD including a “Connection/Turn-on Charge” also known
27 as an activation fee.

28
29 **15. Q. DOES THAT CONCLUDE YOUR TESTIMONY?**

30 **A.** Yes, it does.

31