

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

WATER SERVICE CORPORATION OF )  
KENTUCKY'S NOTICE OF INTENT TO FILE ) CASE NO. 2013-00237  
AN APPLICATION FOR RATE ADJUSTMENT )

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ATTORNEY GENERAL'S POST-HEARING BRIEF

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Respectfully submitted,  
JACK CONWAY  
ATTORNEY GENERAL



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JENNIFER BLACK HANS  
GREGORY T. DUTTON  
ASSISTANT ATTORNEYS GENERAL  
1024 CAPITAL CENTER DRIVE  
SUITE 200  
FRANKFORT KY 40601-8204  
(502) 696-5453  
FAX: (502) 573-1005

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Comes now the intervenor, the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention, and states as follows for his post-hearing brief in the above-styled matter.

**INTRODUCTION**

Water Service Corporation of Kentucky (“WSCK” or “the Company”) is a wholly owned subsidiary of Utilities, Inc. (“UI”).<sup>1</sup> UI is a privately-held corporation that owns over 70 small water and/or sewer systems that provide service to approximately 270,000 customers in 15 states.<sup>2</sup> Water Service Corporation (“WSC”) is an affiliated service company that provides both operational and management services to all subsidiaries.<sup>3</sup> Since December 2012, UI has been owned by Corix Utilities, a limited liability company whose ultimate principal investor is a Canadian investment management company.<sup>4</sup>

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<sup>1</sup> Direct Testimony of Yap, page 2, line 14.  
<sup>2</sup> Direct Testimony of Yap, page 3, lines 4-6.  
<sup>3</sup> Direct Testimony of Lupton, page 4.  
<sup>4</sup> Direct Testimony of Yap, page 3, line 7.

On 27 September 2013 the Company filed its application requesting a rate increase of \$228,789 or 10.87% in pro forma water sales revenue, based on a test year ending December 31, 2012.<sup>5</sup> WSCK later revised the requested rate increase to \$236,802.<sup>6</sup> WSCK serves 6507 total customers distributed between Bell County (5900 customers) and Hickman County (607 customers).<sup>7</sup> WSCK's requested rate increase would amount to a \$36.39 annual increase to WSCK's ratepayers' bills. By operation of statute,<sup>8</sup> the Commission suspended implementation of the proposed rates through and including 26 March 2014.<sup>9</sup> The statutory suspension period under KRS 278.190(2) expired 26 March 2014, but WSCK - as part of a Response to Intervenor's Motion to Dismiss - waived its right to implement the proposed rates until the conclusion of this case.<sup>10</sup>

Pursuant to KRS 367.150(8), the Attorney General of the Commonwealth of Kentucky ("AG") intervened on behalf of WSCK ratepayers. The Commission also granted intervention to Hickman County Fiscal Court<sup>11</sup> and the City of Clinton.<sup>12</sup> Andrea Crane, an independent revenue expert contracted by the Attorney General, made recommendations based on her evaluation of documents produced by WSCK and the testimony of WSCK's witnesses. Ms. Crane recommended the Commission limit

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<sup>5</sup> Direct Testimony of Yap, page 3, lines 14-22.

<sup>6</sup> Corrected WSCK Rebuttal Schedules filed 4 April 2014, LY-R6-Rev.

<sup>7</sup> AG 1-1; AG Exhibit 7.

<sup>8</sup> KRS 278.190(2) in relevant part states "the Commission may... defer the use of the rate, charge, classification, or service, but not for a longer period than five (5) months beyond the time when it would go into effect if an historical test period is used."

<sup>9</sup> 18 October 2013 Order, page 1, paragraph 1.

<sup>10</sup> 22 November 2013 Motion to Amend the Procedural Schedule, at 7.

<sup>11</sup> 16 October 2013 Order.

<sup>12</sup> 14 November 2013 Order.

rate case expense recovery to the average of the actual costs incurred in the last two WSCK rate proceedings; continue to disallow certain indirect costs allocated to WSCK, including costs for corporate labor; continue to disallow depreciation expense and interest expense associated with Project Phoenix; retain the Company's current depreciation rates; and decrease WSCK's rates by \$118,438 to achieve an 88% operating ratio margin.<sup>13</sup> An Informal Conference was held on 1 April 2014, during which time various inconsistencies and errors in the Company's rebuttal testimony and schedules were identified by Commission staff.<sup>14</sup> Subsequently, the individual responsible for preparing and defending WSCK's rate application was fired on 2 April 2014.<sup>15</sup> The Commission held a public hearing on 9 April 2014 during which Ms. Crane and WSCK's remaining witnesses were made available for questioning.

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<sup>13</sup> Direct Testimony of Crane, page 5, line 7 to page 6, line 12.

<sup>14</sup> Memorandum Re: Informal Conference of 1 April 2014.

<sup>15</sup> Video Transcript ("VT") at 10:24:38-10:26:40.

## ARGUMENT

WSCK, as the applicant utility, bears the burden of proof to show “that an increase of rate or charge is just and reasonable.”<sup>16</sup> WSCK has failed to meet its burden of proof to demonstrate that the revenue increase it proposes will result in fair, just and reasonable rates.<sup>17</sup> Furthermore, evidence was provided to suggest that WSCK’s current earnings actually exceed the 88% operating ratio allowed by the Commission. Therefore, and as explained in the testimony filed by the Attorney General and summarized herein, the Attorney General recommends a revenue decrease of \$118,438.<sup>18</sup>

### **1. LACK OF EVIDENCE DEMONSTRATING BENEFITS TO KENTUCKY RATEPAYERS AND COMMISSION PRECEDENT NECESSITATES DENYING RECOVERY OF PROJECT PHOENIX EXPENSES AND DEPRECIATION**

Project Phoenix was UI’s implementation of new financial and customer systems, including installation of new hardware and software.<sup>19</sup> The financial systems went live on 3 December 2007 and customer systems went live on 2 June 2009.<sup>20</sup> The total cost of Project Phoenix to UI was \$21.12 million.<sup>21</sup>

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<sup>16</sup> *Kentucky-American Water Company v. Commonwealth ex rel. Cowan*, Ky., 847 S.W.2d 737 (1993).

<sup>17</sup> See KRS 278.190 “At any hearing involving the rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the utility...”; See also *Energy Regulatory Commission v. Kentucky Power Co.*, 605 S.W.2d 46, 50 (Ky. App. 1980). (At such hearing and through the Commission proceeding, the municipal utility seeking the rate adjustment bears the burden of showing that the proposed adjustment is reasonable.)

<sup>18</sup> Updated Schedules of Andrea Crane, ACC-13, line 11; AG Exhibit 20.

<sup>19</sup> Direct Testimony of Baryenbruch, page 4.

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

<sup>21</sup> *Id.* at 6.

WSCK seeks to recover \$76,685 in this rate case for depreciation associated with Project Phoenix.<sup>22</sup> In the 2010 WSCK rate case, the Attorney General argued “WSCK has not shown the reasonableness of the expense and the corresponding benefits to the ratepayers of WSCK.”<sup>23</sup> The Attorney General’s arguments today are the same and remain valid. Expenses, even those having a minimal effect on operating income, must be borne by investors unless such expenses are proven beneficial to ratepayers in furnishing utility service.<sup>24</sup> The Commission has previously stated its belief that the interest of the shareholders **AND** the customers should be balanced and protected.<sup>25</sup> The mere inclusion of an expense amount in an application creates no presumption of benefit.<sup>26</sup> WSCK has failed here, as it has in its last two rate cases before this Commission, to produce evidence to show that UI examined the potential benefits Project Phoenix would have for WSCK and Kentucky ratepayers.

When WSCK sought to recover depreciation expenses from this Commission in 2008, the Commission found

“Based on the evidence of record, it is apparent that Utilities did not perform a benefit analysis of Project Phoenix to ascertain the potential financial impact or to identify any benefits Project Phoenix would provide to each of its operating subsidiaries, in particular Water Service. As pointed out by the AG, it is Water Service’s burden to document that the cost of Project Phoenix is reasonable and to identify the benefits the

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<sup>22</sup> ACC-8; AG Exhibit 20.

<sup>23</sup> Case No. 2010-00476, *In the Matter of Application of Water Service Corporation of Kentucky for an Adjustment of Rates*, Attorney General’s Post-Hearing Brief, page 3.

<sup>24</sup> Case No. 9842, *In the Matter of Kentucky-American Water Company*, at 22 (Ky. PSC July 18, 1986); *see also* Case No. 10498, *In the Matter of Columbia Gas of Kentucky, Inc.*, at 30 (Ky. PSC Oct. 6, 1989).

<sup>25</sup> Case No. 91-370, *In the Matter of: Application of the Union Light, Heat and Power Company to Adjust Electric Rates*, at 31 (Ky. PSC May 5, 1992). (emphasis added)

<sup>26</sup> *Energy Regulatory Commission v. Kentucky Power*, 605 S.W.2d 46, 50 (Ky.App. 1980).

computer software will provide to the ratepayers of Water Service.... For these Reasons, the Commission finds that Water Service has failed to demonstrate that the allocated Project Phoenix costs are reasonable.”<sup>27</sup>

The Commission ruled the same way in 2010, WSCK’s last rate case. There, the Commission found

“Our review of the record in this proceeding and in WSKY’s last rate proceeding indicates no new evidence that requires us to alter our earlier findings. In the last proceeding, we expressly noted the failure of UI to perform an analysis to show that Project Phoenix benefited WSKY’s ratepayers.”

Both Commission Orders found a lack of evidence demonstrating a benefit to Kentucky ratepayers. As there has been no new evidence introduced in this rate case demonstrating benefit of Project Phoenix to Kentucky ratepayers, the Commission should continue to disallow recovery of depreciation from Project Phoenix.

In 2010, the Attorney General argued “There has not been a demonstration that a reasonable utility of comparable size would spend in excess of a half-million dollars on software similar to that contained in Project Phoenix.”<sup>28</sup> This statement still rings true today. WSCK witness Mr. Baryenbruch was hired to support the Company’s request for depreciation expenses associated with Project Phoenix.<sup>29</sup> However, other than stating that he believes the cost of Project Phoenix to be justified, Mr. Baryenbruch

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<sup>27</sup> Case No. 2008-00563, *In the Matter of: Application of Water Service Corporation of Kentucky for an Adjustment of Rates*, at 6 (Ky. PSC Nov. 9, 2009); AG Exhibit 3.

<sup>28</sup> Case No. 2010-00476, Attorney General’s Post-Hearing Brief, page 3.

<sup>29</sup> Direct Testimony of Baryenbruch, pages 3-4.



provided no new evidence to support the Company's claim.<sup>30</sup> Commission Staff requested that Mr. Baryenbruch provide a copy of the "study" referenced in Mr. Baryenbruch's testimony that purports to support the costs being claimed in this case for Project Phoenix.<sup>31</sup> In response, the Company indicated that there is no "study" but rather Mr. Baryenbruch only conducted a "review."<sup>32</sup> Moreover, this review was based primarily on discussions with Mr. Lubertozi, UI's Chief Regulatory Officer and on Mr. Baryenbruch's professional experience.<sup>33</sup> In fact, WCK then acknowledged that "Mr. Baryenbruch's review did not entail an audit or highly detailed data-gathering process."<sup>34</sup> Mr. Baryenbruch did a cursory review of documents, drafted his direct and rebuttal testimony, and that's the full extent of Mr. Baryenbruch's efforts to demonstrate any benefit to Kentucky ratepayers from Project Phoenix.

The only new material submitted by WCK in its supplemental testimony were the two management audits attached to Mr. Baryenbruch's testimony.<sup>35</sup> However, Mr. Baryenbruch admitted during cross-examination that neither of the audits were conducted *for the benefit of Kentucky rate payers* and neither of the audits specifically looked at the potential benefits of Project Phoenix.<sup>36</sup> The Company did not provide any new and relevant documents to support benefits to Kentucky ratepayers from Project

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<sup>30</sup> VT 14:07:22-14:27:36 "The two documents - my direct testimony and my rebuttal testimony - are my work product."

<sup>31</sup> PSC 2-19.

<sup>32</sup> *Id.*

<sup>33</sup> *Id.*

<sup>34</sup> PSC 2-20; AG Exhibit 16.

<sup>35</sup> See Schumaker audits attached to the end of Mr. Baryenbruch's rebuttal testimony.

<sup>36</sup> VT 14:30:20-14:31:28.

Phoenix and Mr. Barynebruch conducted a brief, cursory review of documents before forming his opinion. This Commission has previously stated, through its Orders, that it expects to see evidence of benefit to Kentucky ratepayers before the Company can recover depreciation from Project Phoenix. WSCK has failed to deliver this evidence yet again. Therefore, WSCK should continue to be disallowed from recovering depreciation associated with Project Phoenix.

**2. THE LACK OF INDEPENDENT MANAGEMENT OF WSCK, WSCK'S INABILITY TO REJECT ALLOCATED COSTS FROM THE PARENT COMPANY, AND COMMISSION PRECEDENT NECESSITATES DENYING RECOVERY OF ALLOCATED EXPENSES**

WSCK is allocated a portion of costs incurred by WSC. Costs incurred by WSC are directly charged to a utility, if applicable.<sup>37</sup> Costs that cannot be directly assigned are allocated based on the Equivalent Residential Connections ("ERCs") of the subsidiaries that benefit from the function being allocated.<sup>38</sup> WSCK does not receive an invoice related to these costs - instead the charges are automatically booked to WSCK through UI's financial accounting system.<sup>39</sup>

***A. Mr. Shambaugh's Study Failed to Carry the Burden of Proof that the Allocated Costs are Reasonable***

Company witness Shambaugh would suggest that his study provides sufficient evidence that economies of scale exist within UI that provide value to WSCK. However, due to Mr. Shambaugh's methodology, his study results are virtually useless.

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<sup>37</sup> Direct Testimony of Lupton, page 4.

<sup>38</sup> *Id.*

<sup>39</sup> *Id.*; PSC 1-28.

Mr. Shambaugh compared several cherry-picked expenses from municipal water utilities to WSCK's expenses. This might have been of some use had there been a baseline from which all the comparisons could be conducted. However, Mr. Shambaugh chose not to use an objective baseline. Instead, he compared the per-customer cost of other utilities to the per-ERC costs of WSCK. Furthermore, he falsely labeled his exhibits; stating that he was using the number of WSCK customers in his comparisons when in fact he was not.<sup>40</sup> Mr. Shambaugh was fully aware that his exhibit was misleading and that he was using ERC's, not the actual number of WSCK customers.<sup>41</sup> This is a covert apples-to-oranges comparison **at best** and calls into question the credibility of Mr. Shambaugh and his study. The credibility of his study is put further at risk when considering that Mr. Shambaugh did not bother to verify the data associated with the Water Districts in his study.<sup>42</sup> The Attorney General recommends discounting Mr. Shambaugh's testimony based on these factors and the testimony of Ms. Crane.

Assuming *arguendo* that Mr. Shaumbaugh's study is found credible, it does not provide evidence that WSCK's allocated costs are reasonable. On the contrary, when actual number of WSCK customers is substituted for ERCs, we see that per customer cost for Officers and Directors salaries is \$9.18 per WSCK customer, highest of all

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<sup>40</sup> Shambaugh Exhibit C; AG Exhibit 13.

<sup>41</sup> VT 14:00:10-14:00:29.

<sup>42</sup> VT 14:06:21-14:06:50; 14:04:15-14:04:25. Mr. Shambaugh was provided with – and never verified – both the number of customers from the Water Districts and the number of WSCK Customers.

utilities Mr. Shambaugh examined.<sup>43</sup> If Mr. Shambaugh's study is examined via an apples-to-apples comparison - number of customers vs. number of customers - we see that WSKY's per customer costs are some of the highest in almost all of the metrics examined. Mr. Shambaugh and his study fail to carry the burden of proving that the allocated costs are reasonable.

***B. UI's Corporate Structure Continues to Prevent WSKY from Exerting any Independent Business Decision-Making***

The Commission's Order issued in WSKY's 2010 rate case states,

"the members of WSKY's Board of Directors also serve as Directors of other UI subsidiaries, including Water Service Corporation. On its face, this arrangement presents an apparent conflict of interest and raises questions about WSKY's willingness to question transactions with Water Service Corporation."<sup>44</sup>

While some recent changes in job titles has taken place within UI, until those changes took place two individuals - Lisa Sparrow and John Stover - constituted the President, CEO, Vice President and Secretary of WSKY's parent companies, while simultaneously holding those positions with WSKY.<sup>45</sup> They even make up the entirety of the Board of Directors for WSKY.<sup>46</sup> When the 2010 WSKY rate case was filed, WSKY would not and could not question transactions with WSC. The same organizational structure that this Commission felt was a conflict of interest in 2011 is still in place today.<sup>47</sup> Furthermore,

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<sup>43</sup> VT 14:05:19-14:05:38

<sup>44</sup> Case No. 2010-00476, *In the Matter of Application of Water Service Corporation of Kentucky for an Adjustment of Rates*, at 9 (Ky. PSC Nov. 23, 2011); AG Exhibit 2.

<sup>45</sup> AG 1-24 (AG Exhibit 9); AG 1-22 (AG Exhibit 10); VT 10:54:55-10:55:20.

<sup>46</sup> AG 1-22 (AG Exhibit 10); VT 10:54:55-10:55:20.

<sup>47</sup> VT 10:56:25-10:56:35.

the contract between WSCK and its parent companies has not been modified since the last rate case.<sup>48</sup>

UI is structured so that its subsidiary companies have virtually no ability to contest, refute, or even review costs allocated to them by the parent company. WSC does not issue an invoice to WSCK.<sup>49</sup> This creates an allocation system that the Commission has previously recognized is

“the product of a less-than-arm's-length transaction that allocates all of the indirect costs incurred by Water Service Corporation without a review clause that would serve as a check and balance system to allow only those reasonable costs that relate to the Water Service operations to be allocated to Water Service.”<sup>50</sup>

There is not even any type of a system in place that would allow for the correction of an allocation that is due to a math error.<sup>51</sup> In short, there is still no independent review of costs allocated to WSCK by the parent company. With regard to this, the 2010 Order states “the record indicates an absence of any independent review of the cost allocations by WSCKY’s Management. In the absence of adequate support for the charges, the Commission disallows allocated indirect costs of \$169,886 from pro forma operating expenses.”<sup>52</sup>

There is no independent review of cost allocations and a conflict of interest still exists within the management structure. WSCK has failed to carry the burden of proof that the indirect cost allocations from Water Service Corporation are reasonable, are

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<sup>48</sup> Staff 2-14(a); VT 10:56:35-10:56:58.

<sup>49</sup> VT 13:37:00-13:37:20; Staff 1-28 Exhibit Y; AG 1-20.

<sup>50</sup> Case No. 2008-00563, at 15 (Ky. PSC Nov. 9, 2009); AG Exhibit 3.

<sup>51</sup> VT 13:46:35-13:46:50.

<sup>52</sup> Case No. 2010-00476, at 12 (Ky. PSC Nov. 23, 2011); AG Exhibit 2.

directly related to providing water service, or benefit the ratepayers of Water Service. Thus, the Commission should continue to disallow corporate labor costs allocated to WSCK. The Commission excluded these costs from the rates paid by Kentucky ratepayers in the last two rate cases, and it should continue to exclude these costs from rates.

### **3. WSCK'S RATE CASE EXPENSE IS UNREASONABLE, IMPROPER AND SHOULD NOT BE RECOVERED IN FULL FROM RATEPAYERS**

Typically the Commission grants the recovery of rate case expenses where adequate documentation exists to demonstrate the reasonableness of the expense.<sup>53</sup> However, the Commission has previously denied recovery of full rate case expenses where 1) “the level of rate case expenses is excessive when compared to the level of requested rate adjustment”<sup>54</sup> and 2) “when the expenses were related to a poorly or improperly prepared rate application.”<sup>55</sup> Both conditions precedent are present in this rate case; therefore, the Commission should deny WSCK’s recovery of all or a significant portion of rate case expense from its ratepayers.

WSCK has requested a total annual revenue increase of \$236,802<sup>56</sup>. The Company has forecasted total rate case costs for this case of \$239,767.<sup>57</sup> Based on the

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<sup>53</sup> Case No. 2009-00428, *In the Matter of: Proposed Adjustment of Wholesale Water Service Rates of the City of Greensburg*, (Ky. PSC Aug.6, 2010).

<sup>54</sup> Case No. 2009-0373, *In the Matter of: Proposed Adjustment of the Wholesale Service Rates of Hopkinsville Water Environment Authority*, at 12-13, (Ky. PSC July 2, 2010).

<sup>55</sup> *Greensburg*, at 5 (Ky. PSC Aug.6, 2010) citing Case No. 8783, *Third Street Sanitation, Inc.*, at 7 (Ky. PSC Nov. 14, 1983).

<sup>56</sup> Corrected WSCK Rebuttal Schedules filed 4 April 2014, LY-R6-Rev.

requested three-year amortization, WSCK is seeking to recover \$79,922 annually related to the current case.<sup>58</sup> Therefore, over the next three years, \$79,922 of the additional \$236,802 WSCK seeks to recover annually from ratepayers is related solely to rate case expense for the current case.<sup>59</sup> That means the **rate case expense for this case would account for a full 33.75% of the increase ratepayers would experience.**<sup>60</sup> **This is more than one-third of the total requested revenue increase.**<sup>61</sup> In Case No. 2009-0373, the applicant was denied full rate case expense recovery because expenses amounted to 11% of the total rate increase.<sup>62</sup> WSCK is seeking triple that amount.

Sufficient evidence exists in this case to find that WSCK's application was both poorly and improperly prepared. To begin, WSCK requested multiple procedural accommodations.<sup>63</sup> WSCK required nearly two full months simply to respond to the Attorney General's Initial Request for Information. WSCK boldly admits that it needed additional time because "activities in other rate cases in other jurisdictions caused difficulties in providing responses by the November 22, 2013, deadline."<sup>64</sup> UI

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<sup>57</sup> LY-R7. In addition, the Company is seeking a three-year amortization of unamortized costs of \$27,505 from its last base rate case.

<sup>58</sup> \$239,767 / 3 years = \$79,922.

<sup>59</sup> This does not include the \$27,505 in unamortized rate case expense from WSCK's last rate case.

<sup>60</sup> \$79,922/\$236,802 = 33.75%

<sup>61</sup> VT 17:57:00-17:58:38. Note that during the Hearing, upon the questioning of Commissioner Breathitt, Ms. Crane confirmed this fact, which remains undisputed by WSCK.

<sup>62</sup> Case No. 2009-0373, *In the Matter of: Proposed Adjustment of the Wholesale Service Rates of Hopkinsville Water Environment Authority*, (Ky. PSC July 2, 2010).

<sup>63</sup> See WSCK's 4 November 2013 Motion to Extend Deadlines and Amend Procedural Schedule, 27 November 2013 Supplemental Information to the Second Motion to Amend the Procedural schedule, and 22 November 2013 Motion to Amend the Procedural Schedule. *See generally* Joint Response to Water Service Corp of Kentucky's Motion to Amend Procedural Schedule and Attorney General, Hickman County Fiscal Courts, and City of Clinton Joint Motion to Dismiss Water Service Corp of Kentucky's Application for Rate Adjustment with Prejudice.

<sup>64</sup> 22 November 2013 Motion to Amend the Procedural Schedule, at 7.

prioritized other rate cases in other jurisdictions to the detriment of this rate case. WSCK missed both the original deadline of 8 November 2013 and the extended 22 November 2013 deadline.<sup>65</sup> WSCK's final request for an extension of time was granted only upon WSCK's agreement to not implement the proposed rates until issuance of a final decision in this case.<sup>66</sup> The Commission even warned the Company that "further requests for extensions of time by WSKY shall result in a dismissal of this case."<sup>67</sup> It then took until 13 December 2013 for WSCK to file responses to the Attorney General's Initial Requests for Information, which was filed by the Attorney General on 25 October 2013. Of note, is the fact that WSCK filed a paltry 62 pages of testimony with its initial application, yet filed 366 pages of rebuttal testimony. Furthermore, the Company witness ultimately charged with preparing and filing the application was fired exactly one week prior to the Hearing after Intervenors and Commission Staff brought to the Company's attention numerous application errors and inconsistencies.<sup>68</sup> The application should have never been filed or at least withdrawn once the Company realized it could not commit proper resources toward this case.

In light of the fact that WSCK has requested excessive rate expense based on an improperly prepared application, the Attorney General recommends one of three actions by the Commission. The Commission can use the average of WSCK's three

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<sup>65</sup> 4 November 2013 WSCK Motion to Extend Deadlines and Amend Procedural Schedule.

<sup>66</sup> 13 December 2013 Order, page 4, paragraph 1 ("Based on WSKY's agreement to not implement the proposed rates prior to issuance of a final decision in this case, WSKY's November 22, 2013 motion to amend the procedural schedule is granted").

<sup>67</sup> 13 December 2013 Order, page 4, paragraph 6.

<sup>68</sup> VT 10:24:38-10:26:40.



previous rate cases and award recovery of \$125,224, as recommended by the Attorney General's Expert witness.<sup>69</sup> The Commission can award \$115,795.50 as a 50/50 sharing of cost by ratepayers and shareholders.<sup>70</sup> Third, if the Commission adopts the Attorney General's recommendation of a rate reduction, then the entire rate expense requested should be denied based on a wholly improper application.

**4. *WSCK has Reversed Its Position on Several Miscellaneous Items During the Course of this Case and the Revised Positions Should be Noted***

***A. Uncollectibles***

In the application, WSCK reflected uncollectible rate bills as a reduction to pro forma water sales revenues instead of as an operating expense. Ms. Crane challenged this classification based on traditional ratemaking policies and the Commission's ruling in WSCK's last rate case.<sup>71</sup> In Mr. Yap's rebuttal testimony, WSCK adopted Ms. Crane's recommendation to treat WSCK uncollectible costs as an operating expense as opposed to an operating revenue reduction.<sup>72</sup> This was confirmed during the Hearing.<sup>73</sup>

***B. Depreciation Rates***

WSCK did not include in its application either a depreciation study or a proposal to adopt new depreciation rates. However, in response to a discovery request the

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<sup>69</sup> Direct Testimony of Crane, page 19. *See also* AG 1-80 (rate case expense table for rate cases in years 2005, 2008, 2010).

<sup>70</sup> Case No. 2013-00148, *Application of Atmos Energy Corporation for an Adjustment of Rates and Tariff Modifications*, at 14 (Ky. PSC Apr. 22, 2014). (Acknowledging as viable approach for ratemaking purposes.)

<sup>71</sup> Direct Testimony of Crane, page 12, lines 14-18.

<sup>72</sup> Rebuttal Testimony of Yap, page 2, lines 15-17.

<sup>73</sup> VT 10:32:00-10:32:09.

company stated “WSCK is proposing to recover expenses for depreciation that is consistent with the 1979 NARUC Study.”<sup>74</sup> Ms. Crane did not support this change in depreciation rates and addressed the issue in her Direct Testimony.<sup>75</sup> Company witness Yap then reasserted in his rebuttal testimony that “WSCK supports basing its depreciation rates and expenses on the 1979 NARUC Study that has been identify (sic) in this case.”<sup>76</sup> However, shortly after Mr. Yap’s employment with WSCK was terminated<sup>77</sup>, the Company filed revised schedules indicating that it would opt to use the depreciation rates that had been previously approved in the Company’s last rate case.<sup>78</sup> Mr. Neyzelman confirmed during cross-examination that the Company reversed its position and no longer seeks to change its depreciation rates.<sup>79</sup>

### *C. Post-Test Year 3% Salary and Wage Increase*

WSCK filed a calculation of salary and benefits on worksheet w/p[b] that included a footnote stating “Salaries Annualized to include an estimated 3% raise effective 4/1/2013.”<sup>80</sup> Based on this information, the Attorney General believed WSCK to be proposing a 3% post-test year salary and wage increase. Ms. Crane offered testimony on this issue.<sup>81</sup> The Company then filed several pages of rebuttal testimony

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<sup>74</sup> AG 2-6.

<sup>75</sup> See generally, Direct Testimony of Crane, page 30, line 6 to page 32, line 5.

<sup>76</sup> Direct Testimony of Yap, page 6, lines 20-21.

<sup>77</sup> Mr. Yap’s employment was terminated on April 2, 2014 and the revised schedules were filed April 4, 2014.

<sup>78</sup> WSCK Corrected Rebuttal Schedules, filed 4 April 2014.

<sup>79</sup> VT 10:51:06-10:51:23.

<sup>80</sup>w/p[b], footnote 1; AG Exhibit 4.

<sup>81</sup> Direct Testimony of Crane, page 14, line 5 to page 14, line 11.

supporting the proposed adjustment.<sup>82</sup> However, during cross-examination of Mr. Neyzelman – who adopted all of Mr. Yap’s testimony and schedules after Mr. Yap’s employment was terminated - the Company revealed that it was not actually proposing a 3% post-test year salary and wage increase. Company witness Mr. Neyzelman further explained that while the footnote was inaccurate, it had never been corrected, despite ample opportunity to do so in the Company’s rebuttal testimony.<sup>83</sup> As a result, either the Company never meant to propose the adjustment but never fixed the error, or the Company decided to accept Ms. Crane’s recommendation to remove the adjustment.

**5. THE COMPANY FAILED TO COMPLY WITH THE COMMISSION’S ORDER IN CASE NO. 2012-00133 AND SHOULD BE PENALIZED UNDER KRS 278.990**

In Case No. 2012-00133, the Commission approved transfer of control of Water Service Corporation to Corix Utilities from Highstar Capital Fund II, L.P.<sup>84</sup> Corix Utilities owns UI. The Commission issued an Order on 13 August 2012 that stated in part “To provide a forum for customers to communicate with utility management, Corix Utilities and Utilities, Inc. shall host annual public meetings in Clinton and Middlesboro, Kentucky, at which the senior officers from the regional office of Utilities,

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<sup>82</sup> Direct Testimony of Yap, page 3, line 13 to page 5, line 16.

<sup>83</sup> VT 10:33:45-10:34:58.

<sup>84</sup> Case No. 2012-00133, *In the Matter of: Joint Application of Corix Utilities (Illinois) LLC; Hydro Star, LLC; Utilities, Inc.; and Water Service Corporation of Kentucky for the Transfer and Acquisition of Control Pursuant to KRS 278.020*, (PSC Aug. 13, 2012).

Inc. that oversees Water Service Corporation's operations will attend and participate."<sup>85</sup> Mr. Haas is a senior officer from the regional office of UI<sup>86</sup> and he oversees Water Service Corporation's operations in Kentucky.<sup>87</sup> Neither Mr. Haas, nor any other senior officer from the Midwest regional office, attended or participated in a public meeting in Clinton or Middlesboro since this Order was issued.<sup>88</sup> Mr. Haas even admitted that as of 9 April 2014 the Company is not in compliance with the Order.<sup>89</sup> The appendix to the 2012-00133 Order makes the Commission's requirements even clearer, simply stating "Corix Utilities and Utilities, Inc. will host annual public meetings in Clinton and Middlesboro to provide a forum for customers to communicate with utility management."<sup>90</sup> Mr. Haas confirmed a second time that the Company is not in compliance with the Commission's Order.<sup>91</sup>

During cross-examination of Mr. Haas, Counsel for WSCK objected and attempted to argue that UI's non-compliance with the Commission's order was not relevant to this general rate case.<sup>92</sup> Wisely, the Chairman overruled Counsel's objection, finding that, the issue of the company's compliance with Commission Orders and prior commitments made were relevant to the current rate case.<sup>93</sup> Thereafter, on re-direct, Counsel for WSCK all but testified for Mr. Haas that in November 2013, at Counsel's

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<sup>85</sup> *Id.* at 11, paragraph 20.

<sup>86</sup> VT 15:40:35-15:40:48.

<sup>87</sup> VT 15:39:59-15:40:05.

<sup>88</sup> VT 15:41:40-15:42:41.

<sup>89</sup> VT 15:45:52-15:45:59.

<sup>90</sup> Case No. 2012-00133, Appendix A, page 3, paragraph 16 (Ky. PSC Aug.13, 2012); AG Exhibit 2.

<sup>91</sup> VT 15:47:57-15:48:05.

<sup>92</sup> VT 15:44:23-15:44:36.

<sup>93</sup> VT 14:44:36-15:44:57.

urging via communications, the Commission Staff waived Ordering Paragraph 20 and Appendix A paragraph 16 pending the conclusion of the rate case.<sup>94</sup> As demonstrated by an evaluation of the communications in question, which the Commission wisely had tendered into the record, not only was Counsel in error regarding the legality of this proposition, Counsel patently misled the Commission and the public regarding these exchanges.

First, the Commission may only speak through its Orders; Commission staff through formal or informal communications may not waive a prior Order of the Commission.<sup>95</sup> Further, to suggest that counsel could approach the Commissioners, without consultation among all intervening parties, and seek such a waiver of Ordering Paragraphs relevant to an on-going rate case, is to condone *ex-parte* communication.<sup>96</sup>

Second, the public records produced after the conclusion of the hearing demonstrate that the Commission staff in no way addressed this issue. Rather, in a dated letter, which was not served on any intervening parties to either this case or the former matter, Counsel for WSCK attempted to bootstrap the annual meeting commitment to any public meetings the Commission may have held in Bell County and

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<sup>94</sup> VT 15:48:20-15:48:56.

<sup>95</sup> KRS 278.390 states in part “Every order entered by the commission shall continue in force until the expiration of the time, if any, named by the commission in the order, or until revoked or modified by the commission, unless the order is suspended, or vacated in whole or in part, by order or decree of a court of competent jurisdiction.”

<sup>96</sup> *Louisville Gas & Electric Co. v. Commonwealth ex rel Cowan*, 862 S.W. 2d 897, 900 (1993), (“an *ex parte* contact is condemnable, when it is relevant to the merits of the proceeding”); Case No. 2003-00115, *In Re: Southeast Telephone, Inc.* (Ky. PSC Dec. 19, 2003) (“when there is an allegation that an improper *ex parte* contact has occurred, the key question is whether the contact in question concerned the “merits” of the proceeding”).

Hickman County.<sup>97</sup> While it appears the Executive Director of the Commission gave WSCK “a pass on the ‘annual’ meeting requirement of paragraph 19 of the August 13, 2012 Order,”<sup>98</sup> that paragraph pertains to meetings between Company officials and the Commission, not meetings between Company officials and the public. Paragraph 20 requires annual meetings with the public, and Commission staff in no way granted WSCK a “pass” on paragraph 20 of the Order.<sup>99</sup>

KRS 278.990(1) states in part “If any utility ...fails to obey an order of the Commission...the utility shall be subject to a civil penalty to be assessed by the commission for each offense not less than twenty-five dollars (\$25) nor more than two thousand five hundred dollars (\$2,500) for each offense.” Company representative Haas has already admitted that the Company is in non-compliance with the Commission’s Order. This Commission has previously penalized utilities under KRS 278.990 for failing to obey its Orders.<sup>100</sup> WSCK should have complied with the Order. A non-recoverable penalty should be required from WSCK for failure to honor its

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<sup>97</sup> 11 April 2014 PSC Filing Documents. See 3 December 2013 Letter from Todd Osterloh, Counsel for WSCK to Jeff DeRouen, Executive Director KPSC.

<sup>98</sup> *Id.* See 3 December 2013 Email from Jeff DeRouen, Executive Director KPSC, to James R. Woods, Legal Staff, KPSC.

<sup>99</sup> *Id.* See 3 December 2013 Email from James R. Woods to Todd Osterloh, counsel for WSCK (“Your other question about public meetings is being discussed. I will get back with you later on that issue”).

<sup>100</sup> Case No. 2007-00185, *In the Matter of: Kentucky American Water Company Alleged Failure to Comply with KRS 278.300(1)*; Case No. 2009-00359, *In the Matter of: Kentucky-American Water Company’s Application for Approval of Payment of Dividend*; Case no 96-037, *In the Matter of Kentucky Power Company d/b/a/ American Electric Power and Bellsouth Telecommunications, Inc. Alleged Failure to Comply with Commission Regulations.*

commitment to ratepayers and failure to comply with the Commission's previous Order.<sup>101</sup>

WSCK is in non-compliance with an Order that directly impacts the ratepayers of Bell and Hickman counties; the exact ratepayers that WSCK now seeks to obtain additional revenue from. The requirement for an annual public meeting was included in the Order due to the terrible relationship between WSCK and its customers. Rates cannot be fair just and reasonable when the company collecting the rates disregards basic customer service requirements installed by the Commission.


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<sup>101</sup> Compliance with the Case No. 2012-00133, 13 August 2012 Order could not be ascertained until the Attorney General was given the opportunity to question Company witnesses through a rate proceeding. Therefore, it is proper to assess penalties in the Commission's Order in this case, as opposed to re-opening Case No. 2012-00133.

## CONCLUSION

The evidence demonstrates that the application of Water Service Corporation of Kentucky overstates its annual revenue requirement. In fact, WSCK is overearning and should receive a *rate decrease* of \$118,438. WSCK has proven that it is a poorly run company with low customer satisfaction. As evidence, note the two Intervenors from Hickman County and the Comments filed by the City Counsel for the City of Middleton. In addition, note that the company needed numerous procedural accommodations and then fired the individual charged with preparing the rate case a mere 6 days before the Hearing commenced. This Commission has repeatedly disallowed recovery of expenses related to project Phoenix and certain allocated costs from UI. The reasons for the Commission's decision in prior rate cases are still present. For these reasons and those stated above, the Attorney General recommends a rate decrease of \$118,438 for Water Service Corporation of Kentucky.

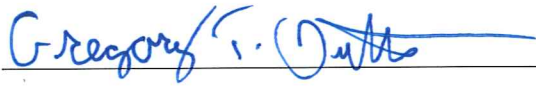
Respectfully submitted,  
JACK CONWAY  
ATTORNEY GENERAL

  
\_\_\_\_\_  
JENNIFER BLACK HANS  
GREGORY T. DUTTON  
ASSISTANT ATTORNEYS GENERAL  
1024 CAPITAL CENTER DRIVE  
SUITE 200  
FRANKFORT KY 40601-8204  
(502) 696-5453  
FAX: (502) 573-1005



*Certificate of Service and Filing*

Counsel certifies that the Attorney General's Post-Hearing Brief is a true and accurate copy of the documents to be filed in paper medium; that the electronic filing was transmitted to the Commission on May 9, 2014; that an original and two copies of the filing will be delivered to the Commission within two business days; and that no party has been excused from preparation by electronic service.

A handwritten signature in blue ink, reading "Gregory S. Datta", is written over a horizontal line.

Assistant Attorney General