

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC PROPOSED)
ADJUSTMENT OF THE WHOLESALE) CASE NO. 2017-00417
WATER SERVICE RATES OF)
LEBANON WATER WORKS)

POST-HEARING BRIEF OF
LEBANON WATER WORKS COMPANY

FILED: June 29, 2018

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I. INTRODUCTION

This case stems from a dispute between a municipal supplier of water, Lebanon Water Works Company (the “Company”) and a water district, Marion County Water District (the “Marion District”), that has purchased water from the municipal supplier for more than 50 years. In early 2017, the Company determined that its present rates were insufficient to meet its current operation and maintenance expenses, service its outstanding debt, and provide working capital for system improvements necessary to maintain safe and reliable service, so it began the contractual process of a rate adjustment to its retail customers and Marion District.

The Company based its rates on historical and budgeted information and determined that rates must generate \$3,438,209, which is an increase of \$798,208. The Company has provided information as current as possible throughout this proceeding to allow the Public Service Commission (the “Commission”) to base its decision on actual operations, not just budgeted or projected information. Since this proceeding was initiated, the Company obtained audited financial information for Fiscal Year Ending June 30, 2017 (“FY 2017”). The FY 2017 Audit Report has been filed into the record. The Company has also supplemented that information with adjustments that have been filed into the record. To facilitate the Commission’s decision in this matter, the Company is providing a chart as

Appendix A to this Brief to compile the Company's most recent financial information and adjustments. This chart shows that, based upon its operations for FY 2017 as adjusted to reflect known and measurable events, the Company requires additional revenue from rates of \$946,252. The Company continues to request only \$798,208, but the actual numbers show the reasonableness of the Company's request.

II. STATEMENT OF THE CASE

The Company, a non-profit local governmental corporation created by an act of the Kentucky General Assembly in 1884, owns and operates facilities that treat and distribute water to the residents of the City of Lebanon, Kentucky (the "City"). It provides water service to approximately 2,600 customers located in and near Lebanon, Kentucky. The City is the Company's sole shareholder and appoints the members of the Company's board of directors. The Board of Directors, however, functions independently and exercises its own discretion in the management and operation of the Company's facilities. The Lebanon City Council retains the authority to fix and regulate the rates charged to the Company's customers.¹

Marion District, a water district organized pursuant to KRS Chapter 74, owns and operates facilities that distribute water for compensation to unincorporated portions of Marion and Nelson Counties, Kentucky. Marion

¹ KRS 96.190(2).

District does not produce its own water but purchases almost all of its water requirements from the Company.²

The Company has been providing water service to Marion District by contract since 1968. The Water Purchase Agreement currently in place was made and entered into on December 23, 1988 (the “Master Agreement”). The Master Agreement has been amended several times, but none of the addendums materially change the contractual relationship or process for a rate adjustment between the Company and Marion District. For the nearly 30 years that the Master Agreement has been in place, the Company has raised rates pursuant to the process set forth in the Master Agreement. Prior to 2017, Marion District had not protested an increase in rates, including two increases of a larger percentage.³

In 2016, the Company launched a review of its expenses to determine if its current rates reflected the full cost of providing service. In December 2016, Daren Thompson, the Company’s Operations and Management Superintendent, notified Marion District’s Manager of this review. By spring 2017, the Company had determined that its present rates were insufficient to meet its current operation and maintenance expenses, service its outstanding debt, and provide working capital for system improvements necessary to maintain safe and reliable service. The Company’s calculations indicated that the single, uniform rate, which applies to all

² Marion District purchases a small amount of water from Campbellsville to serve a limited number of customers.

³ See Memorandum in Support of Motion to Assign Burden of Proof at 6 (Ky. PSC Jan. 31, 2018).

customers within Lebanon's city limits and includes Marion District, should be increased to produce sufficient revenues to cover the increased cost of service. This increase includes an 8.9 percent increase to the meter charge and a 34 percent increase to the volumetric component of the single, uniform rate.

On July 10, 2017, the Lebanon City Council conducted the first reading of Ordinance 2017-06 which would implement the proposed adjustment to the Company's single, uniform rate. Prior to this first reading, Company officials met with Marion District officials to explain the Company's proposal. Despite receiving notice of the first reading, Marion District officials failed to attend the Lebanon City Council meeting or submit any formal protest or challenge to the proposed rates.

Between July 10, 2017 and September 11, 2017, Company officials met with Marion District officials to provide additional information regarding the proposed rate adjustment. At Marion District's request, the Company asked the Lebanon City Council to delay a second reading of Ordinance 2017-06 an additional 30 days to permit additional discussions with Marion District regarding the rate adjustment. Company officials also provided informational briefings in open forums, to various public officials in city and county government, and to various community organizations.

On September 11, 2017, the Lebanon City Council conducted its second reading of Ordinance 2017-06. Marion District officials did not attend these proceedings, did not present any evidence to the Lebanon City Council regarding the proposed rate adjustment, nor did they make any formal protest of the proposed rate adjustment to the Lebanon City Council.

The Company immediately implemented the rates contained in Ordinance 2017-06 to its retail customers. The implementation of these rates for Marion District, however, was delayed 60 days pursuant to the terms of the Master Agreement.

On September 13, 2017, the Company filed with the Commission notice of the proposed rate that the Lebanon City Council had reviewed and approved in accordance with the procedures set forth in the Master Agreement.⁴ This action followed the guidance that the Commission had previously provided to municipal utilities that had water purchase agreements with Commission-regulated water utilities.⁵

On September 25, 2017, Marion District filed with the Commission a written protest and requested that a formal proceeding be initiated to investigate the

⁴ In its notice, the Company indicated that the proposed rate would be implemented for service provided on and after November 15, 2017. This implementation date is consistent with the Master Agreement's requirement that the final determination of the Lebanon City Council would not take effect until 60 days after the final reading and passage of an Ordinance approving the single, uniform rate to permit Marion District adequate time to obtain an adjustment of its rates for service pursuant to KRS 278.015. Direct Testimony of Daren Thompson, Exhibit 1 at 7.

⁵ See Letter from Beth O'Donnell, Executive Director, Kentucky Public Service Commission to All Municipal Utilities Providing Wholesale Utility Service to Jurisdictional Public Utilities (Oct. 16, 2007).

reasonableness of the proposed rate. In its protest, Marion District stated that it was unable “to ascertain whether the proposed adjustment is consistent with the methodology set forth in the water purchase contract that Lebanon and MCWD have executed.”⁶ It questioned whether the proposed rate “reflects Lebanon’s actual cost of providing service” to Marion District and cited nine (9) specific concerns regarding the rate adjustment.⁷

On November 13, 2017, the Commission established this proceeding to review “the reasonableness of the proposed rates” and suspended the operation of the proposed rates as assessed to Marion District for a period of five (5) months. On February 28, 2018, the Commission issued an Order in which it assigned the burden of proof in this matter to the Company and established a procedural schedule. Because the procedural schedule did not permit either party to file written testimony, the Company moved to modify the procedural schedule. On March 19, 2018, the Commission issued an Order granting the Company’s Motion and setting forth a procedural schedule that provided for multiple rounds of discovery, testimony and rebuttal testimony, and a Hearing. Pursuant to KRS 278.190(2), the Company placed its proposed rates, with the exception of the proposed rate case expense surcharge, into effect for Marion District on April 16,

⁶ Letter from Kaelin G. Reed, counsel for Marion County Water District, to John S. Lyons, Acting Executive Director, Kentucky Public Service Commission (Sept. 19, 2017) (“Reed Letter”) at 1.

⁷ *Id.* at 1-2.

2018—seven (7) months after the rates for retail customers had been increased.

The Companies have responded to four (4) rounds of discovery from Commission Staff, three (3) rounds of discovery from Marion District, and provided testimony, rebuttal testimony, and live testimony at the Hearing on June 20, 2018. Through this, the Company has shown that its rate to Marion District is fair, just, and reasonable.

III. ARGUMENT

A. The Fiscal Year Ending June 30, 2017 Should Be Used As The Test Period To Review The Reasonableness Of The Proposed Rates.

In conducting its review, the Commission should use FY 2017 as the test period to determine the reasonableness of the Company's proposed rates. The Company's operations for FY 2017 are the most representative of the Company's current operations and those in the Company's immediate future. They are known, easily measured, and fully documented in the record. Use of this period is reasonable and consistent with existing legal precedent and accords with Marion District's position as set forth in its original objection to the proposed rates.

The purpose of using a test period is to establish with a reasonable degree of accuracy revenue and expenses that a public utility will experience during the

period when new rates are in effect.⁸ Courts have consistently held a “test period should be based on the utility’s most recent actual experience with such adjustments as will make the test period reflect typical conditions in the immediate future.”⁹

FY 2017 is the most recent period for which actual figures for the Company’s operations are available. More significantly, FY 2017 followed a year of transition in which the Company experienced numerous changes in its operations and is therefore more representative of the Company’s present operations and its operations in the immediate future. During the Fiscal Year ending June 30, 2016 (“FY 2016”), the Company hired a new Operations and Management Superintendent while continuing to employ its existing Superintendent pending his retirement. It also hired several new employees to replace long-time employees who were also nearing retirement and initiated a number of new construction projects and other initiatives to improve service reliability and improve efficiency. The full effects of these efforts were not realized until FY 2017, and they will continue to affect the Company’s operation for the immediate future.

⁸ 73B C.J.S. *Public Utilities* § 105 (2010). See also *Evansville v. Southern Indiana Gas & Electric Co.*, 339 N.E.2d 562, 568 (“The test year concept assumes that the operating results during the test period are sufficiently representative of the time in which new rates will be in effect to provide a reliable testing vehicle for new rates.”).

⁹ *Letourneau v. Citizens Utilities Co.*, 259 A.2d 21, 23 (Vt. 1969).

The use of FY 2017 as the test period to evaluate the reasonableness of the proposed rates is consistent with Marion District's position in this proceeding. In its letter of September 25, 2017 in which it requested Commission review of the proposed rates, Marion District objected to the use of FY 2016 as the test period upon which to review those rates. It specifically expressed its concerns regarding the use of FY 2016¹⁰ as test period as well as the Company's use of budgeted expenses for FY 2018 rather than information contained in the completed audit report for FY 2017 operations. Charles White, Marion District's witness who analyzed the proposed rates, relied heavily upon the Company's FY 2017 operations to develop his analysis.¹¹

The record of this proceeding contains substantial information regarding FY 2017 operations upon which the Commission can conduct a thorough and complete review. This information includes:

- An Independent Auditor's Report of the Company's Financial Statements for June 30, 2017 and June 30, 2016;¹²
- The Adjusted Trial Balance for FY 2017;¹³

¹⁰ In his letter requesting Commission review of the proposed rates, one of the concerns that Marion District's counsel expressed with the proposed rates was the "[u]se of a test period in which it [the Company] employed two General Managers during a transition." Letter from Kalin G. Reed, Counsel for Marion District, to John S. Lyons, Acting Executive Director, Kentucky Public Service Commission (Sept. 19, 2017) at 2. FY 2016 was the time period in which the Company employed two general managers.

¹¹ For example, see Direct Testimony of Charles M. White at 3.

¹² Response of Lebanon Water Works Company to Marion County Water District's Request for Information, Item 11-1.

¹³ Response of Lebanon Water Works Company to Commission Staff's Second Request for Information, Item 3(b).

- A Detailed Breakdown of each Item in the 2017 Income Statement by trial balance revenue and expense subaccounts;¹⁴ and
- A Detailed Description of Selected Revenue and Expense Accounts.¹⁵

In addition, the Company's current Superintendent provided lengthy testimony on the Company's operations in FY 2017 and the current fiscal year.

While the Company has referred to its FY 2016 operations in its effort to develop the proposed rates, its use of FY 2016 operations does not mandate the Commission's use of FY 2016 as the test period to evaluate the reasonableness of those rates. The Company has not expressly proposed that the Commission use FY 2016 as the test period. Unlike regulated public utilities, the Company is not required to select a test period upon which to base its proposed rates.¹⁶ The Commission's guidance to municipal utilities on revising rates to public utilities is in fact silent on the selection of a test period.¹⁷ To the extent that the Company originally relied upon FY 2016 operations to develop its rates, this reliance does

¹⁴ Response of Lebanon Water Works Company to Commission Staff's Third Request for Information, Item 2.

¹⁵ Response of Lebanon Water Works Company to Commission Staff's Third Request for Information, Item 5.

¹⁶ The Company developed the proposed rates without consideration of any proceeding before the Commission. Unlike regulated utilities, the Company was not required to develop an application for submission to the Commission. The Commission's practice allows for a municipal utility to file only a tariff sheet setting forth its proposed rates to implement its rates. *See* Letter from Beth O'Donnell, Executive Director, Kentucky Public Service Commission to All Municipal Utilities Providing Wholesale Utility Service to Jurisdictional Public Utilities (Oct. 16, 2007). KRS 278.192 requires the Commission to permit "a utility to utilize either an historical test period of twelve (12) consecutive calendar months, or a forward-looking test period corresponding to the first twelve (12) consecutive calendar months the proposed increase would be in effect after the maximum suspension provided in KRS 278.190(2)." 807 KAR 5:001, Section 16, requires a utility to file an application for general rate adjustment based upon the selected historical test period. As a city-owned water company, the Company is not a "utility," *see, e.g., McClellan v. Louisville Water Company*, 351 S.W.2d 197 (Ky. 1961), neither the statute nor the regulation applies to the Company.

¹⁷ *See* Letter from Beth O'Donnell, Executive Director, Kentucky Public Service Commission to All Municipal Utilities Providing Wholesale Utility Service to Jurisdictional Public Utilities (Oct. 16, 2007).

not require either the Company or the Commission to turn a blind eye or deaf ear to more current and potentially more reliable financial information. The Company has acknowledged throughout this proceeding that its FY 2016 operations are not generally reflective of its current operations and that numerous adjustments were necessary to FY 2016 operations to more accurately reflect the Company's current operations.¹⁸

To the extent that a more recent period of operations exists that more accurately reflects the Company's current operations and those in the immediate future, due process requires that the Commission use such period in determining the reasonableness of the proposed rates. "[A] valid test period must be based upon the utility's most recent actual experience, with adjustments for all known changes affecting costs and revenues for the immediate future. . . . [T]he rate maker may not rely on out-of-date information when more recent actual experience, which shows a substantial disparity between earlier forecasts and the rate of return actually earned, is available. *Potomac Electric Power Co. v. Public Service Com.*, 380 A.2d 126, 133 (D.C. Ct. App. 1977).¹⁹

¹⁸ Response of Lebanon Water Works Company to Commission Staff's Third Request for Information, Item 3(b) ("[T]he Company did not develop its Revenue Requirements based on the Fiscal Year 2016 Income Statement."); Hearing Video Transcript 1:22:00 P.M. (June 20, 2018).

¹⁹ See also *Southern New England Tel. Corp. v. Public Utilities Co.*, 282 A.2d 915, 919 ("Since a test period is employed to show what the probable operating and financial condition of the company will be in the immediate future, in order that rates may be fixed which will compensate the company for all operating expenses and provide it with a fair return, the test year must be representative of the conditions which will prevail in the immediate future when the rates will be effective. This test period must be based on the most recent actual experience of the company, with adjustments made for all known changes affecting costs and revenues in the immediate future which

B. Revenue Requirements Adjustments

The evidence of record clearly dictates that, if FY 2017 is used as the test period to assess the reasonableness of the Company's proposed rates, several adjustments to the FY 2017 operations are necessary. These adjustments are discussed below.

1. Penalties and Garbage Collection Fees

During FY 2017, the Company received approximately \$35,886 in revenue from penalties and late payment fees. None of these revenues was received from Marion District. The Company did not assess any penalty to Marion District during FY 2017. Mr. White testified that the Commission should consider this revenue in determining the reasonableness of the proposed rates.²⁰

The Company agrees that, if the current rate structure remains in effect and Marion District is assessed the uniform rate that is applied to **all customers** as required by the Master Agreement, penalty revenue received from **all customers** should be considered in determining the reasonableness of the proposed rates. However, if the Commission elects to disregard the Master Agreement's requirement for a uniform rate and to establish a different rate for Marion District that is based solely upon the Company's cost to serve Marion District, these

are not conjectural and which are not so remote in time that they might destroy the representative character of the test year.") (citations omitted).

²⁰ Direct Testimony of Charles M. White at 6.

revenues should not be considered as they are unrelated to the Company's provision of water service to Marion District.

Similarly, during FY 2017, the Company received \$11,424 as compensation for its collection of garbage fees for the Marion County Fiscal Court.²¹ These fees should be accorded the same ratemaking treatment accorded penalties and late payment fees.

2. Water Service to the City of Lebanon

During FY 2017, the Company provided 3,700,000 cubic feet of water to the City of Lebanon in exchange for the City's treatment of the sludge from the Company's water treatment plant and other benefits. In his testimony, Mr. White (i) characterized the transaction as the provision of free water service to the City; (ii) recommended that the Commission impute to the Company revenue from the "sale" of this water, which he calculated to be \$92,438; and (iii) recommended that the Commission consider this imputed revenue in determining the reasonableness of the proposed rates.²²

The Company acknowledges that the transaction should be reported in its records and should be considered when reviewing the reasonableness of the proposed rates. The transaction, however, is not the provision of free water service, but an exchange of services between the Company and the City. In

²¹ Rebuttal Testimony of Daren Thompson at 11-12.

²² Direct Testimony of Charles M. White at 6.

exchange for water service, the City provides for the treatment of 540,000 gallons of sludge from the Company's water treatment plant. Mr. Thompson testified that a conservative estimate of the fair market value of this service is approximately \$64,980.²³ To the extent that the Commission recognizes revenues from the transaction by imputing income to the Company, it must also recognize the expense of the sludge treatment service that the Company is effectively purchasing through its provision of water service to the City.²⁴

While the Company acknowledges that the expense and revenue aspects of the transaction should be reflected on its books, the Company's provision of water service to the City is consistent with existing law.²⁵ The Company and the City have openly engaged in this practice for the past 24 years. Nothing has been hidden from the public. As Mr. Thompson noted in his testimony, both entities have benefitted from the practice. In return for the provision of water service to the City, the Company has been able to more easily and efficiently deal with the disposal of water treatment plant sludge than most other water utilities of

²³ Rebuttal Testimony of Daren Thompson at 11-12; Hearing Video Transcript 10:07:20 – 10:08:00 P.M. (June 20, 2018).

²⁴ As an alternative to recording the revenues and expenses associated with this exchange of services, the Commission can remove the expenses associated with the Company's provision of treated water to the City. Mr. Thompson testified that the Company's cost to produce water was \$1.25 per 1,000 gallons. Hearing Video Transcript 9:34:16 – 9:35:47 A.M. (June 20, 2018). Using that cost, approximately \$34,597.40 should be deducted from FY 2017 operating expenses. First, cubic feet are converted to gallons. $(3,700,000 \times 7.480519 = 27,677,920)$ gallons of water, with 7.480519 being the conversion rate for cubic feet to gallons). Next, the cost is calculated. $(27,677,920 \text{ gallons} \times \$1.25/1,000 \text{ gallons} = \$34,597.40)$.

²⁵ See OAG 84-147 (“[I]ndependent of a statute the right of a city to furnish water free for municipal and charitable purposes ‘can hardly be doubted.’”) (citing 12 McQuillin, *Municipal Corporations* § 35.37g (3rd ed.)).

comparable size. Since the Hearing in this matter, the Company has begun discussions with the City to memorialize the arrangement in a written agreement.

3. Purchased Water Expense

During FY 2018, the Company began purchasing water from Campbellsville pursuant to a Water Purchase Contract (“Campbellsville Contract”). After exploring several options to obtain a supplemental source of water, the Company and its Board of Directors determined that purchasing water from Campbellsville was the best solution to the Company’s supply issues.²⁶ The additional water supply will allow the Company the flexibility to shut down all or a portion of its water treatment plant to perform maintenance that is long overdue.

The Campbellsville Contract imposes a minimum purchase requirement of 300,000 gallons of water per day (“GPD”). For each 100,000 GPD increase, the per 1,000 gallon rate decreases. Annually, the Company must choose its minimum daily purchases. Because the wholesale rate is not reduced if the Company purchases more than the selected amount, it behooves the Company to accurately estimate the volume of water that it will need to purchase so it can obtain the benefit of the lower wholesale rate. After considering the planned maintenance projects at the Water Treatment Plant, the Company agreed to purchase 400,000 GPD for the first year. The Company will revisit the minimum daily purchase

²⁶ Direct Testimony of Daren Thompson at 11; Hearing Video Transcript 9:34:40 A.M. (June 20, 2018).

amount annually to optimize its minimum daily purchase amount depending upon the circumstances existing at that time.

When the Company signed the Campbellsville Contract, the Contract provided for the rate of \$3.96 per 1,000 gallons if 300,000 GPD was purchased and \$3.36 per 1,000 gallons if 400,000 GPD was purchased. The Company consequently reported in its Response to Question 2B of the Commission Staff's Request for Information dated February 28, 2018 that the annual cost to the Company is \$490,560 if 400,000 GPD is purchased ($400,000 \times 365 \times \3.36) and \$433,620 if 300,000 GPD is purchased ($300,000 \times 365 \times \3.96). Pursuant to the Campbellsville Contract, Campbellsville recently re-calculated the rates based on its current cost of service. After this re-calculation, the new rate that Campbellsville will charge the Company is \$3.46 if 300,000 GPD is purchased and \$2.99 if 400,000 GPD is purchased. This results in an annual cost to the Company of \$436,540 if 400,000 GPD is purchased ($400,000 \times 365 \times \2.99) and \$378,870 if 300,000 GPD is purchased ($300,000 \times 365 \times \3.46). Because of this known and measurable change, the Company has reduced its original Purchased Water Expense adjustment by \$54,020. It now seeks a Purchased Water Expense adjustment of only **\$436,540**.

Because of the water purchased from Campbellsville, the Company's chemical and power costs will decrease. Based on the incremental costs of

chemicals and power, the Company has calculated a reduction in its water treatment plant expenses of **\$39,733**. The Company's Revenue Requirements reflect these estimated savings.

Mr. White argues that the purchase of 400,000 GPD from Campbellsville should lead to reductions in the purchased power, pump station and filter plant, and chemical costs by approximately 18%. This projection is incorrect. A significant portion of the Company's purchased power costs are due to demand charges. Accordingly, the Company's purchased power costs do not necessarily increase or decrease linearly when it increases or decreases its kilowatt hour electric use. Mr. White also offers no support to decrease chemical or pump station and filter plant costs. As stated in the Rebuttal Testimony of Daren Thompson, the Company continues to believe that savings at the Water Treatment Plant will not exceed \$39,733.

4. Health Insurance Expense

In its request for Commission review of the proposed rates, Marion District cites as one of its concerns the "[i]nclusion of 100% of the costs of health benefits payable to Lebanon's employees" and suggests that the Company is attempting to recover through the uniform rate excessive employee health insurance costs. The record in this proceeding demonstrates the exact opposite. Rather than incurring excessive employee health insurance costs, the Company has embarked upon

aggressive cost control measures to reduce expenses related to employee health insurance costs and to ensure that employees have “skin in the game” so that they become more cost conscious of their health care decisions.

In the last three completed fiscal years, the Company’s health insurance costs have decreased significantly. In the Fiscal Year ending June 30, 2015, the Company’s annual health insurance premium was \$219,324. In FY 2016, the Company’s annual health insurance premium was \$242,544. In FY 2017, the Company reduced its health insurance expense to \$188,400.

In an effort to control costs, the Company has made significant changes to the health insurance plan that it offers its employees. First, the Company obtained proposals from different insurance companies. Second, it chose a more affordable plan (one which requires its employees to pay a higher deductible amount). Third, the Company implemented a Flexible Spending Account through which employees can elect to withhold a portion of their pre-tax salary for qualifying medical expenses, and a Health Reimbursement Account (“HRA”).

Additionally, the Company decreased its health insurance costs by requiring employees with family health insurance coverage to pay a portion of the health insurance premiums. Beginning in Fiscal Year 2018, employees contributed 10% of family coverage premiums. Beginning in Fiscal Year 2019, employees will

contribute 15% of family coverage premiums.²⁷ The Company’s approach of gradually increasing employee contributions for health insurance costs is consistent with the principles set forth in Commissioner Robert Cicero’s Comments to the Kentucky Chamber of Commerce 2018 Energy Conference.²⁸

5. Depreciation

In its request for Commission review of the proposed rates, Marion District voiced concerns about the Company’s “[u]se of aggressive depreciation schedules for transmission lines and other capital improvements which are inconsistent” with Commission ratemaking practices.²⁹ In his testimony, Mr. White repeats these concerns and asserts that the Company was not using the appropriate useful lives to determine its depreciation expense.³⁰

The Company acknowledges that the Commission presently uses “Depreciation Practices for Small Water Utilities” to determine the useful lives of water utility assets. This publication, which the National Association of Regulatory Commissioners (“NARUC”) published in 1979, contains a suggested range of useful lives for various water plant assets. The Commission has recently

²⁷ Implementation of the Commission’s policy requiring employees to contribute 21% and 32%, respectively, of single and family healthcare coverage would not achieve its intended result of healthcare cost reduction. Due to steps taken by the Company, however, its healthcare costs have already decreased significantly. If the Company had retained its old health insurance plan and required employee contributions of 21% and 32%, the Company would still be spending a greater amount on health insurance expenses than under the Company’s current health insurance plan.

²⁸ Robert J. Cicero, “Comments at the Kentucky Chamber of Commerce Energy Conference” (Jan. 18, 2018) at 4, available at https://psc.ky.gov/agencies/psc/speeches/cicero/VC_Cicero_KYChamber_Energy_Conference_1-18-18.pdf.

²⁹ Reed Letter at 2.

³⁰ Direct Testimony of Charles M. White at 5.

held that the mid-point of these ranges should be used to establish a water utility's depreciation expense.³¹

While the Company does not agree that the use of this publication is appropriate or reasonable or that the Commission's reliance upon the mid-point of the publication's useful life ranges will result in an accurate assessment of an asset's useful life, it will for purposes of this proceeding accede to the Commission's practice. In response to a request from Commission Staff, the Company recalculated its depreciation expense using a useful life based upon the NARUC publication's mid-point.³² The results of this recalculation are reflected in **Appendix B** to this Brief. The recalculation reflects a depreciation expense of \$637,438, or \$62,228 more than the depreciation expense level of \$575,210 reported in the Company's FY 2017 financial statements.³³

The recalculation results are affected by two adjustments to FY 2017 levels. First, depreciation expense for assets placed into service during FY 2017 is normalized to reflect a full year of depreciation. Such action is consistent with the

³¹ See, e.g., *Alternative Rate Adjustment Filing of Marion County Water District*, Case No. 2016-00163 (Ky. PSC Nov. 10, 2016).

³² Response of Lebanon Water Works Company to Commission Staff's Third Request for Information, Item 9, Exhibit 9-1.

³³ Response of Lebanon Water Works Company to Marion County Water District's Request for Information, Exhibit 11-2.

Commission's historic ratemaking practices.³⁴ Second, the recalculation takes into account assets that were placed into service after the end of FY 2017.

The Commission has historically permitted the recovery of depreciation expense on post-test period additions to utility plant for water districts and other non-profit local governmental corporations. In Case No. 2016-00163,³⁵ the Commission adopted Commission Staff's recommendation to include in the calculation of a water utility's depreciation expense for ratemaking purposes depreciation on water main replacements that had not been constructed at the time of the utility's application for rate adjustment but were completed prior to the issuance of a Commission Staff report on the application. In making its report, Commission Staff stated:

At the time of Staff's review, Marion District had completed the main replacement at the major creek crossing and one of the secondary crossings. The total cost of these projects was \$42,905. Because these projects had been completed at the time of Staff's review, their costs are known and measurable and may be recovered through the rates authorized in this proceeding.³⁶

³⁴ See, e.g., *Application of Shelby Energy Cooperative, Inc. For An Increase In Its Retail Rates*, Case No. 2016-00434 (Ky. PSC July 31, 2017 (approving electric utility's proposed adjustment to normalize depreciation); *Application of Cannonsburg Water District For (1) Approval Of Emergency Rate Relief and (2) Approval Of The Increase In Nonrecurring Charges*, Case No. 2011-00217 (Ky. PSC June 4, 2012) (adopting Commission Staff recommendation to normalize depreciation on various assets placed into service during test period);

³⁵ *Alternative Rate Adjustment Filing of Marion County Water District*, Case No. 2016-00163 (Ky. PSC Nov. 10, 2016).

³⁶ Staff Report on Marion County Water District at 27 (filed Aug. 11, 2016 in *Alternative Rate Adjustment Filing of Marion County Water District*, Case No. 2016-00163 (Ky. PSC)).

Similarly, in Case No. 2016-00325,³⁷ the Commission adopted Commission Staff's recommendation to permit a water utility rate recovery of depreciation expense on a building purchased more than eleven months after the end of the test period.³⁸

The Commission afforded similar treatment to a water district in Case No. 2017-00338.³⁹ In that proceeding, the Commission established rates that allowed recovery of depreciation expense on a water transmission main and pumping station that had not received the required regulatory approvals at the time of the utility's application for rate adjustment. Although the record in that proceeding is unclear as to the date when the facilities in question were actually completed and placed in service, the record clearly shows that the utility did not have the required regulatory approvals to begin construction of those facilities until almost eleven (11) months after the end of the test period used to evaluate the utility's rates.⁴⁰

³⁷ *Electronic Application of North Mercer Water District For Rate Adjustment Made Pursuant To 807 KAR 5:076*, Case No. 2016-00325 (Ky. PSC May 19, 2017).

³⁸ Staff Report on North Mercer Water District at 13-14 (filed Mar. 22, 2017 in *Electronic Application of North Mercer Water District for Rate Adjustment Made Pursuant To 807 KAR 5:076*, Case No. 2016-00163 (Ky. PSC)). In its application, North Mercer Water District proposed a test period ending December 31, 2015. The building in question was purchased after December 22, 2017 – the date on which the Commission authorized North Mercer Water District to purchase the building. See *Application of North Mercer Water District For A Certificate of Public Convenience And Necessity To Acquire A Building and Make Minimal Adaptations Thereto*, Case No. 2016-00392 (Ky. PSC Dec. 22, 2016).

³⁹ *Electronic Application of U.S. 60 Water District of Shelby and Franklin Counties For An Alternative Rate Adjustment*, Case No. 2017-00338 (Ky. PSC Mar. 21, 2018).

⁴⁰ The utility filed its application for rate adjustment with the Commission on September 7, 2017. The utility filed its application for a certificate of public convenience and necessity to construct the water transmission main and pumping station on September 28, 2017. See *Electronic Application of U.S. 60 Water District of Shelby and Franklin Counties For A Certificate of Public Convenience And Necessity To Construct and Finance Pursuant To KRS 278.020 and KRS 278.300*, Case No. 2017-00323 (Ky. PSC filed Sept. 28, 2017). Notice of the Kentucky Division of Water's approval of the proposed facilities was not filed with the Commission until November 2, 2017. The Commission did not issue a certificate of public convenience and necessity for the proposed facilities until November 10, 2017. In reviewing the reasonableness of the utility's proposed rate adjustment, the Commission used a test period ending December 31, 2016. In its report on the utility's proposed rate adjustment, Commission Staff recommended that test period depreciation expense be adjusted to reflect depreciation on the facilities. Staff

In light of this past precedent, the Commission should consider in reviewing the reasonableness of the Company's proposed rates not only the depreciation expense associated with all assets that were in service as of the end of FY 2017, but also that associated with three construction projects completed after the end of FY 2017 but during the pendency of the current proceeding. These projects are:

Project	Completion Date	Total Cost	Annual Depreciation Expense
Water Treatment Plant Filter Rehab Project	08/08/2017	\$62,839	\$8,977
Water Treatment Plant Clearwell Access and Valve Repair Project	05/31/2018	\$192,250	\$25,390
Campbellsville Transmission Main	03/05/2018	2,534,957	\$40,554

While the Commission has in many instances recognized post-test period additions and permitted adjustments to test-period depreciation expenses to reflect those additions, it has also expressed a preference that all such aspects of the utility's operations, including all revenues and expenses, also be adjusted to reflect changes that occurred during the post test-period.⁴¹ Throughout this proceeding, the Company has repeatedly updated its filings in an effort to comply with that preference.

Report on U.S 60 Water District at 9-10 (filed Feb. 8, 2018 in *Electronic Application of U.S. 60 Water District of Shelby and Franklin Counties For An Alternative Rate Adjustment*, Case No. 2017-00338 (Ky. PSC filed Sept. 7, 2017))

⁴¹ *Notice of Adjustment of the Rates of Kentucky-American Water Company Effective on February 2, 1989*, Case No. 10481, Order at 5 (Ky. PSC Aug. 22, 1989).

6. CERS

The Company is a participating employer of the County Employees' Retirement System ("CERS"). During FY 2017, CERS participating employers were required to contribute 18.68 percent of each employee's wages to the CERS. Based upon the Company's covered employee payroll for FY 2017 of \$611,592, the Company contributed approximately \$114,245 to CERS for FY 2017.

The Kentucky Retirement System recently announced that the required contribution rate for employers participating in the CERS would be 21.48 percent effective July 1, 2018.⁴² The Commission has previously held that changes in the CERS employer contribution rate are known and measurable changes and should be considered when reviewing the reasonableness of employee pensions and benefits expense.⁴³ Applying the new required contribution rate to the Company's FY 2017 covered payroll results in a required employer contribution of \$131,370, an increase of \$17,125 to the Company's CERS contribution in FY 2017.⁴⁴

7. Repairs and Maintenance

In his testimony, Mr. Thompson identified several repair and maintenance projects to which the Company has committed since FY 2017 and which will be

⁴² See <https://kyret.ky.gov/Employers/Pages/Contribution-Rates.aspx> (last visited June 28, 2018).

⁴³ See, e.g., *Application of Northern Kentucky Water District For An Adjustment of Rates*, Case No. 2015-00143 (Ky. PSC Jan. 15, 2016); *The Application of Hardin County Water District No. 1 for a General Rate Adjustment Effective On and After December 2, 2006*, Case No. 2006-00410 (Ky. PSC Aug. 2, 2007)

⁴⁴ $\$611,592 \times 21.48\% = \$131,370$. $\$131,370 - \$114,245 = \$17,125$.

performed on an recurring basis to ensure the service reliability and continuity, and maintain or improve water quality.⁴⁵ These projects include:

- Annual cleaning and disinfection of the clear-well structure and pump suction areas at the Company's Calvary Water Treatment Facility at an annual cost of \$16,075;
- Quarterly and annual preventative maintenance on the Calvary Water Treatment Facility's filters at an annual cost of \$19,465;
- Testing and repairing circuit breakers and motor controls at the Calvary Water Treatment Facility at an annual cost of \$10,000;
- Megger testing on electric motors at an annual cost of \$1,500; and,
- Weekly hauling sludge from the Calvary Water Treatment Facility WTP to City of Lebanon's Wastewater treatment plant at an annual cost of \$23,400

Mr. Thompson testified that these services were necessary to address the Company's continued postponement of routine maintenance in critical service areas. The Company has provided invoices and service agreements⁴⁶ to demonstrate that these expenses are known and measureable, will continue to be incurred annually for several years, and are necessary for the provision of quality

⁴⁵ Direct Testimony of Daren Thompson at 23-24; Hearing Video Transcript 10:12:12 – 10:16:01 A.M. (June 20, 2018).VT: 06/20/2018; 10:12:12 – 10:16:01

⁴⁶ Response of Lebanon Water Works Company to Marion County Water District's Post-Hearing Request for Information, Item 2.

water to Marion District and its other customers. These expenses require an adjustment to FY 2017 Repairs and Maintenance of **\$70,440**.

8. GIS Adjustment

In 2017 the Company updated its GIS mapping system. It entered into an Interagency Agreement with the City of Lebanon and the Marion County Property Valuation Administrator to update the base mapping. The three entities contracted to pay a third party to provide updated aerial photography of Marion County. Each is obligated to pay \$16,667 annually for each of the next three years. In addition, the Company acquired GIS Asset Management Solution, a mapping upgrade to its GIS system. It will be required to pay an annual license fee of \$4,000 annually for GIS Asset Management Solution. This license fee is a recurring expense necessary for the provision of water service. FY 2017 Miscellaneous expense should be increased to reflect this additional expense.

C. A Debt Service Coverage Ratio of 1.25 Should Be Applied to All Company Debt.

The Company is entitled to a Debt Service Coverage (“DSC”) ratio of 1.25 on all of its debt. Such a DSC ratio is required by Ordinance and is necessary to provide the Company working capital to perform system improvements necessary to maintain safe and reliable service.

Ordinance No. 91-9 contains very detailed and specific requirements concerning DSC and other covenants that the City of Lebanon and the Company

are required to uphold to avoid defaulting on the outstanding Bonds.⁴⁷ All Bonds issued by the City of Lebanon, including the 1992 Bonds, 1997B Bonds, and the 2002 Bonds were issued pursuant to the requirements of Ordinance No. 91-9. When Citizens National Bank (“CNB”) “stepped into the shoes” of the original bondholder (USDA, Rural Development and its predecessors), it assumed the covenants and other protections afforded the original bondholder, including the 1.25 DSC requirement.

The Company’s KIA assistance agreements do not specify any DSC requirements. Nevertheless, because the Company has pledged its revenues to KIA as security for the KIA loans, Ordinance No. 91-9 requires that the Company maintain a DSC ratio of 1.25 times the maximum Annual Debt Service on all long-term loans, including the CNB loans and the KIA loans. The Affidavit of William P. Thompson, President and CEO of CNB, attached as **Exhibit 8-1** to the Company’s Response to the Commission Staff’s Third Request for Information, confirms that CNB requires a DSC of 1.25 times the maximum Annual Debt Service on all loans outstanding payable from pledged revenues.

The application of the DSC ratio on KIA loans is consistent with the Commission’s past practices in rate cases involving water districts. In 2013,

⁴⁷ Ordinance No. 91-9 was attached as **Exhibit 7** to the Direct Testimony of Daren Thompson dated March 21, 2018.

Marion District refinanced three RD debts by obtaining a loan from CNB.⁴⁸ In Marion District's most recent Alternative Rate Adjustment filing, the Commission included the annual debt payments on all long-term debts owed by Marion District in calculating the DSC requirements.⁴⁹ These included RD, CNB, and KIA loans.⁵⁰ Staff stated: "The DSC method, as historically applied by the Commission, includes an allowance for additional working capital that is equal to the minimum net revenues required by a district's lenders that are above the district's average annual debt payments."⁵¹ Accordingly, Staff determined that Marion District's additional working capital should be stated at \$29,051 by multiplying Marion District's average annual principal and interest payments on its RD, CNB, and KIA loans by 120% (Marion District's DSC ratio as required by its RD bond resolution).⁵²

D. The Company's Rate Design Should Not Be Modified.

The Company provides water to Marion District under the Master Agreement's contractual framework. The Company has not proposed to change

⁴⁸ *Application of the Marion County Water District for Authority to Enter Into a Loan Agreement with Citizens National Bank of Lebanon, Kentucky*, Case No. 2013-00093, Order at 1 (Ky. PSC Apr. 8, 2103) (listing three RD loans that were refinanced).

⁴⁹ *Alternative Rate Adjustment Filing of Marion County Water District*, Case No. 2016-00163, Staff Report at 33-35 (Ky. PSC Aug. 11, 2016). The Commission approved the DSC used in the Staff Report in its Nov. 10, 2016 Order.

⁵⁰ *Id.* at 33.

⁵¹ *Id.* at 34.

⁵² *Id.* at 34-35. The Commission has applied this same practice to calculate a working capital allowance for numerous other non-profit local governmental entities that have issued debt to Rural Development or the Kentucky Rural Finance Corporation and the Kentucky Infrastructure Authority. See, e.g., *Electronic Application of West Carroll Water District For Rate Adjustment*, Case No. 2017-00244 (Ky. PSC Apr. 24, 2018); *Application For Rate Adjustment of Nebo Water District*, Case No. 2016-004335 (Ky. PSC June 5, 2017); Staff Report on Martin County Water District (May 22, 2018) (filed in *Application of Martin County Water District For An Alternative Rate Adjustment*, Case No. 2018-00017 (Ky. PSC filed Jan. 16, 2018)).

this contractual framework. Accordingly, the Company does not have the burden to show that the rate design is reasonable; instead, Marion District has the burden of proof to show that the rate design is unreasonable. In effect, Marion District is requesting that the Commission modify the Master Agreement. The Commission has previously held that where a party seeks to modify the contract, it bears the burden to show the contract unreasonable.⁵³

Regardless, the rate design of the Company's rates is reasonable and should not be modified. Marion District has presented no evidence to show that the Company's current rate design is unreasonable. Although Marion District has attempted to manipulate the numbers to show that the rate increase has a disparate impact, the fact remains that the Company is simply seeking to impose the same increase of the meter and volumetric charges as it has already imposed to its retail customers.

Under these proposed rates, Marion District will fund approximately the same percentage of total revenue from rates as water usage percentage. For FY 2017, as Marion District cited, it used approximately 56.24% of water sold.⁵⁴ For the same time period, it provided 54.95% of total revenue from rates. If the numbers upon which the proposed rates are based are used, Marion District will be

⁵³ *Proposed Revision of Rules Regarding the Provision of Wholesale Water Service By the City of Versailles To Northeast Woodford Water District*, Case No. 2011-00419, Order at 12 (Ky. PSC Aug. 12, 2014); *East Clark County Water District v. City of Winchester, Acting By and Through Winchester Municipal Utilities Commission*, Case No. 2005-00322, Order at 2 (Ky. PSC Apr. 3, 2006).

⁵⁴ Direct Testimony of Charles M. White at 6.

required under the proposed rates to provide 58.32% of the revenue from rates. If the most current numbers shown in Exhibit 1 of the Nicholas Rebuttal Testimony are used, Marion District will be providing 52.7% of the revenue from rates.

E. The Company’s Rate Case Expense Should Be Recovered Through The Proposed Rate Case Expense Surcharge.

The Company is entitled to recover all rate case expense incurred in this proceeding. The recovery of rate case expense is consistent with longstanding judicial⁵⁵ and Commission precedent.⁵⁶ The U.S. Supreme Court has held that “[e]ven where the rates in effect are excessive, on a proceeding by a commission to determine reasonableness, we are of the view that **the utility should be allowed its fair and proper expenses for presenting its side to the commission.**”⁵⁷

The Company’s rate case expenses are reasonable. The Company has submitted invoices for all of the Company’s \$162,695.30 rate case expense, which include detailed time entries for all expenses incurred.⁵⁸ Further, many of the bills and time entries from Stoll Keenon Ogden PLLC contain discounts or write-offs in recognition of the amount of the rate case expense. The Commission has

⁵⁵ See, e.g., *Driscoll v. Edison Light & Power Co.*, 307 U.S. 104, 120-121 (1939) (“Even where the rates in effect are excessive, on a proceeding by a commission to determine reasonableness, we are of the view that the utility should be allowed its fair and proper expenses for presenting its side to the commission.”); *West Ohio Gas Co. v. Public Utilities Comm’n*, 294 U.S. 63, 74 (1935); *Southern Bell Tel. & Tel. Co. v. Georgia Public Service Com.*, 49 S.E.2d 38 (Ga. 1948).

⁵⁶ See, e.g., Case No. *Proposed Adjustment of the Wholesale Water Service Rates of the City of Owenton, Kentucky*, Case No. 98-283, Order (Ky. PSC Feb. 22, 1999).

⁵⁷ *Driscoll v. Edison Light & Power Co.*, 307 U.S. 104, 120-121 (1939) (emphasis added).

⁵⁸ Invoices were submitted as **Exhibit 20** and **21** of the Direct Testimony of Daren Thompson filed March 21, 2018; **Exhibit 5** of the Rebuttal Testimony of Daren Thompson filed on June 8, 2018; and as **Exhibit 20-1, 20-2, and 20-3** of the Supplemental Response of Lebanon Water Works Company to Commission Staff’s Second Request for Information, Item 20 filed on June 27, 2018.

previously found that a similar rate case expense amount was reasonable in a municipal rate proceeding.⁵⁹ The amount of rate case expense incurred by the Company is comparable to the rate case expense incurred in other municipal rate proceedings.⁶⁰

At the hearing, Vice Chairman Cicero raised concerns about the Company's and Marion District's combined rate case expenses, stating: "\$200 thousand is a lot of money to be spending when we're talking about a rate increase of \$798 thousand . . . [that is] close to 25% of the total that is being sought."⁶¹ The Company, however, has proposed a rate increase to generate \$798,208 *annually*. Because the Company will receive these rates annually for at least three (3) or four (4) years, the dispute between the Company and Marion District represents \$2.4 or \$3.2 million, not just \$798,208.

All rate case expense was incurred as a result of Marion District's initiation of this proceeding. Although the Company met with representatives of Marion District on multiple occasions to explain the need for the proposed increase and to reach some accommodation, Marion District chose litigation over negotiation and compromise. Mr. Jimmy Mudd, Marion District's General Manager, stated

⁵⁹ *Proposed Adjustment of the Wholesale Water Service Rates of the City of Pikeville, Kentucky*, Case No. 2002-00022, Order at 15 (Ky. PSC Oct. 18, 2002).

⁶⁰ *Proposed Adjustment of the Wholesale Water Service Rates of the City of Augusta*, Case No. 2015-00039 (Ky. PSC May 19, 2016); *Proposed Adjustment of the Wholesale Rates of the City of Danville*, Case No. 2014-00392 (Ky. PSC Aug. 13, 2015); *Proposed Adjustment of the Wholesale Service Rates of Hopkinsville Water Environment Authority*, Case No. 2009-00373, Order (Ky. PSC July 2, 2010).

⁶¹ Hearing Video Transcript 12:00:03 P.M. (June 20, 2018).

Marion District thought there “wasn’t any negotiation to be made.”⁶² The Commission has held that a municipal utility’s rate case expense should be recovered from only the wholesale customer:

The Commission regulates only a portion of Owenton’s operations. It does not regulate Owenton’s retail operations nor is Owenton required to obtain Commission approval for those rates. As the costs associated with Commission review are clearly associated only with Owenton’s wholesale rate, the Commission finds that these costs should be attributed to Owenton’s wholesale operations only.⁶³

Furthermore, the recovery of the Company’s rate case expense through the proposed rate case expense surcharge is appropriate. First, because the rate case expense must only be recovered from Marion District, a surcharge appropriately ensures that retail customers do not shoulder the burden of the rate case expense. Second, as the Company explained in its response to Question No. 20 of the Commission Staff’s Second Request for Information, the recovery of rate case expense through a surcharge is not a novel concept—the municipal utilities of Owenton⁶⁴, Hopkinsville,⁶⁵ and Greensburg⁶⁶ have or have had a rate case expense surcharge included in their tariffs.

⁶² Hearing Video Transcript 2:11:24 P.M. (June 20, 2018).

⁶³ *Proposed Adjustment of the Wholesale Water Service Rates of the City of Owenton, Kentucky*, Case No. 98-283 (Ky. PSC Feb. 22, 1999) at 9.

⁶⁴ *Id.* The Owenton tariff was attached to the Company’s Response to the Commission Staff’s Second Request for Information, Question No. 20(A) as **Exhibit 20-1**.

⁶⁵ *Proposed Adjustment of the Wholesale Service Rates of Hopkinsville Water Environment Authority*, Case No. 2009-00373, Order (Ky. PSC July 2, 2010). The Hopkinsville tariff was attached to the Company’s Response to the Commission Staff’s Second Request for Information, Question No. 20(A) as **Exhibit 20-2**.

⁶⁶ *Proposed Adjustment of Wholesale Water Service Rates of the City of Greensburg*, Case No. 2009-00428, Order (Ky. PSC Aug. 6, 2010). The Greensburg tariff was attached to the Company’s Response to the Commission Staff’s Second Request for Information, Question No. 20(A) as **Exhibit 20-3**.

Additionally, recovering rate case expenses in a line item surcharge is more transparent and fair than including rate case expenses in base rates. It prevents the municipal utility from recovering amounts in excess of the actual expense incurred. This could occur if the amount is included in the general wholesale rate and the municipal utility does not adjust rates again for a significant period of time. The use of a line item surcharge to recover rate case expense is easier for the wholesale supplier and customer, as well as the Public Service Commission, to track. It provides a level of predictability for both wholesale supplier and customer.

The Company also proposed the use of a surcharge based upon actual expense to avoid potential problems associated with the inclusion of an estimated rate case expense in proposed rates. If the proposed wholesale rates included estimated rate case expense and were permitted to become effective without any Public Service Commission proceeding, the proposed rate would have been based upon costs that had not been incurred and would have been unfair to the wholesale customer. Based upon prior proceedings in which the Public Service Commission has limited recovery of rate case expense to the amount set forth in the original filing,⁶⁷ if the Company underestimates rate case expense, it will not fully recover its actual costs.

⁶⁷ See *Electronic Application of Monroe County Water District For Rate Adjustment Pursuant to 807 KAR 5:076*, Case No. 2017-00070 (Ky. PSC Jan. 12, 2018) at 16. The Public Service Commission has indicated that a utility's efforts to periodically report its actual rate case expense, even when such efforts are in direct response to Commission Staff's requests for information are insufficient to support a level that is higher than the estimated level.

Based upon the precedent established in Case No. 2014-00392,⁶⁸ in which the Commission refused to allow recovery of a municipal utility's rate case expense because the municipal utility had failed to make the request in its initial filing with the Commission, the Company filed a separate surcharge to comply with the holding in Case No. 2014-00392 and provide the Commission and Marion District with sufficient notice of the proposed surcharge.

IV. CONCLUSION

The Company's requested rate adjustment is fair, just, and reasonable. For the reasons stated herein and throughout this proceeding, the Company requests the Commission permit it to continue with its use of the single, uniform rate structure that has been consistently applied over the last 30 years whereby Marion District and the Company's retail customers pay the same rate.

In particular, the Company requests the Commission approve its proposed rate adjustment which increases the Meter Charge to **\$7.35** and the volumetric rate to **\$3.35** per 100 cubic feet. These rates will generate additional annual revenues of \$798,208 from all customers.

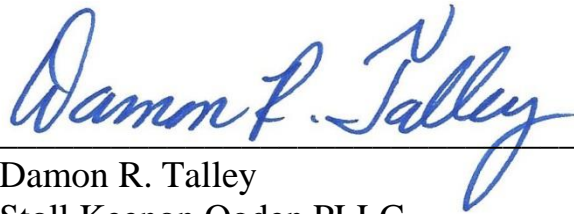
It has also suggested that the utility may amend its application to seek recovery of a higher level of actual expenses. The Company regards this suggestion as problematic since an amendment to the original filing will effectively reset the statutory review period, require the utility to provide notice of the amendment in accordance with KRS 278.180, and lengthen the time before the issuance of a final decision.

⁶⁸ *Proposed Adjustment of the Wholesale Rates of the City of Danville*, Case No. 2014-00392 (Ky. PSC Aug. 13, 2015).

Although the record clearly demonstrates the need for approximately 20% more revenue from rates than requested, the Company remains committed to the rates set forth in its filing of September 13, 2017.

Dated: June 29, 2018

Respectfully submitted,



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CERTIFICATE OF SERVICE

In accordance with 807 KAR 5:001, Section 8, I certify that Lebanon Water Works Company's June 29, 2018 electronic filing of this Post-Hearing Brief is a true and accurate copy of the same document being filed in paper medium; that the electronic filing has been transmitted to the Commission on June 29, 2018; that there are currently no parties that the Commission has excused from participation by electronic means in this proceeding; and that an original and one copy in paper medium of this Post-Hearing Brief will be delivered to the Commission on or before July 3, 2018.



Damon R. Talley

APPENDIX A

	Original Revenue Requirements Determination*	2017 Actual **	Adjustment to 2017 Actual	Notes	Proforma 2017
Operating Revenue					
Charges for Services	2,640,000	2,672,537	92,438	A	2,764,975
Penalties		35,886		B	35,886
Rental Income		0		C	0
					0
Total Operating Revenue	2,640,000	2,708,423	92,438		2,800,861
					0
Operating Expenses					0
Purchased Water	450,827	0	436,540	D	436,540
Power	230,000	225,559			225,559
Pump Station and Filter Plant	69,300	61,871	64,980	E	126,851
Chemicals	170,000	185,077			185,077
Maintenance and Repairs	201,500	136,318	70,440	F	206,758
Salaries	615,200	643,122			643,122
Fringe Benefits - Employees	328,300	356,421	17,125	G	373,546
Payroll Taxes	47,100	46,549			46,549
Directors' Fees	12,600	12,600			12,600
Insurance	49,100	49,265			49,265
Office Supplies and Expense	34,000	59,709			59,709
Outside Services	65,400	59,927			59,927
Bad Debt Expense	0	1,410			1,410
Miscellaneous	31,800	25,434	20,667	H	46,101
WTP Savings	0	0	-39,733	I	-39,733
					0
Total Operation and Maintenance Expenses	2,305,127	1,863,262	570,019		2,433,281
					0
Depreciation	600,000	575,210	62,228	J	637,438
					0
Total Operating Expenses	2,905,127	2,438,472	632,247		3,070,719
Utility Operating Income	-265,127	269,951	-539,809		-269,858

Pro Forma Operating Expenses	2,905,127	2,438,472	632,247		3,070,719
Plus: Annual Debt Principal & Int	532,037	436,363	121,733	K	558,096
Debt Coverage (Working Capital)	63,844	109,091	32,117		139,524
Total Revenue Requirement	3,501,008	2,983,926	786,097		3,768,339
Less: Other Operating Revenue	53,400	11,424		L	11,424
Non-Operating Revenue					
Interest Income	9,400	9,802			9,802
Revenue Required From Rates	3,438,208	2,962,700	786,097		3,747,113
Less: Revenues From Sales at Present Rates	2,640,000	2,708,423	92,438	A	2,800,861
Required Revenue Increase	798,208	254,277	691,975		946,252

Notes

*	See Response of Lebanon Water Works Company to Commission Staff's First Request for Information, Item 1(b). The categories listed correspond to the FY 2016 Financial Statement and to Commission Staff Hearing Exhibit No. 1. In the original calculation, the Company included a separate category for "WTP Plant Savings." In categorizing the expenses, Commission Staff apparently allocated these savings to another category. Accordingly, the original calculation as presented in this Appendix does not separately report the expected savings from the reduced volume of water treatment at the Lebanon Water Treatment Plant due to purchases from Campbellsville.
**	Source: 2017 Audit Report. See Response of Lebanon Water Works Company to Marion County Water District's First Request for Information, Item 11, Exhibit 11-1.
A	Reflects imputed water sales to City of Lebanon. See Post-Hearing Brief of Lebanon Water Works Company at 14, n.24 (filed June 29, 2018).
B	The Company stipulates that penalties should be included in Revenue Determination
C	No rental income was earned in FY 2017 nor since. See Exhibit 3-1 of the Response of Lebanon Water Works Company to Commission Staff's Third Request for Information, Item 3. See also Hearing Video Transcript 1:03:08 - 1:03:47 P.M. (June 20, 2018).
D	No water was purchased during FY 2017; however, obligation under water purchase agreement with Campbellsville required purchases upon completion of Campbellsville Water Transmission Main in March 2018. See Response of Lebanon Water Works Company to Marion District's First Request for Information dated April 12, 2018, Question No. 15.
E	Reflects the cost of sludge treatment services received from City of Lebanon: \$64,980. Rebuttal Testimony of Daren Thompson at 9.
F	Reflects contracts for maintenance services to water treatment plant: \$70,440. See Rebuttal Testimony of Holly Nicholas at 5; Direct Testimony of Daren Thompson at 22-24.
G	Reflects increase in CERS employer contribution rate from 18.68% to 21.48%. See Rebuttal Testimony of Daren Thompson at 21. (2017 Payroll used to calculate adjustment.)
H	Reflects annual license fee of \$4,000 for GIS Asset Management Solution and \$16,667 annual payment related to Interagency Agreement for GIS mapping system. See Direct Testimony of Daren Thompson at 24-25.
I	Reflects reduction in Chemical and Purchase Power Expense due to lower volume of water treated at Company WTP. See Response of Lebanon Water Works Company to Marion County Water District's Supplemental Request for Information, Item 3.
J	Reflects normalization of depreciation expense for assets placed into service in FY 2017 and depreciation expense for assets placed into service after 6/30/2017 using NARUC useful life midpoints. See Response of Lebanon Water Works Company to Commission Staff's Third Request for Information, Item 9, Exhibit 9-1.
K	See Company's Response to Commission Staff's Third Request for Information, Question No. 8(c).
L	The original calculation also considered tap fees and developer contributions. As these items are contributions to capital and not considered revenue, they were not considered when determining the Company's revenue requirements based upon FY 2017 operations.

APPENDIX B

Depreciation Methodology	Amount	Reference
Audit Report for FY 2017	\$575,210	A
Revenue Requirements	\$600,000	B
Assets in Service in FY 2017	\$708,354	C
Assets in Service in FY 2018	\$806,086	D
NARUC Midpoint Depreciation	\$637,438	E

A. The Audit Report for FY 2017 was provided as **Exhibit 11-1** to the Company's Response to Marion District's First Request for Information dated April 2, 2018.

B. The depreciation expense included in the Revenue Requirements was shown in Spreadsheet No. 1 attached to Question No. 2 of the Company's Response to Commission Staff's First Request for Information dated February 28, 2018.

C. The depreciation expense for the assets in service in FY 2017 is shown on the Depreciation Schedule Worksheet filed as **Exhibit 1** to the Rebuttal Testimony of Daren Thompson filed on June 8, 2018. The column titled "2018 Depreciation" provides a full year of depreciation for all assets in service in FY 2017. The Lebanon useful lives were used to calculate depreciation.

D. The depreciation expense for assets in service in FY 2018 is shown on the NARUC Depreciation Schedule Worksheet filed as **Exhibit 9-1** to the Company's Response to Commission Staff's Third Request for Information dated June 8, 2018. The column titled "Pro-Forma 2018 Depreciation" provides a full year of depreciation for assets that have already been placed into service in FY 2018. The Lebanon useful lives were used to calculate depreciation.

E. The annual depreciation expense using the NARUC midpoint for the useful lives was shown on **Exhibit 9-1** of the Company's Response to Commission Staff's Third Request for Information dated June 8, 2018.