

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF ATMOS )  
ENERGY CORPORATION FOR AN ) Case No.  
ADJUSTMENT OF RATES ) 2018-00281

**ATTORNEY GENERAL'S RESPONSES TO DATA REQUESTS  
OF THE KENTUCKY PUBLIC SERVICE COMMISSION STAFF**

Comes now the intervenor, the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention, and submits the following responses to data requests of the Kentucky Public Service Commission Staff in the above-styled matter.

Respectfully submitted,

ANDY BESHEAR  
ATTORNEY GENERAL



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*Certificate of Service and Filing*

Counsel certifies that the foregoing is a true and accurate copy of the same document being filed in paper medium with the Commission within two business days; that the electronic filing has been transmitted to the Commission on February 27, 2019; that there are currently no parties that the Commission has excused from participation by electronic means in this proceeding. Counsel further certifies that the responses set forth herein are true and accurate to the best of his knowledge, information, and belief formed after a reasonable inquiry.

This 27<sup>th</sup> day of February, 2019.



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Assistant Attorney General

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WITNESS/RESPONDENT RESPONSIBLE:

Lane Kollen

QUESTION No. 1

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Refer to the Direct Testimony of Lane Kollen (Kollen Testimony) at pages 7-14, in which he recommends that depreciation rates be reduced to reflect the use of the Average Life Group (ALG) procedure as opposed to the Equal Life Group procedure (ELG).

- a. State whether Mr. Kollen contends that the ELG procedure should never be used to calculate the depreciation expense of investor-owned utilities for ratemaking purposes and, if so, explain each basis for his contention.
- b. If it is not Mr. Kollen's contention that the ELG procedure should never be used to calculate the depreciation expense of investor-owned utilities for ratemaking purposes, identify those situations in which he contends that use of the ELG procedure would be appropriate and explain why it would be appropriate in those circumstances.
- c. On page 10, Mr. Kollen states, "[u]nder the ELG procedure, particularly if it is adopted after the utility historically has used the ALG procedure, the capital recovery periods are accelerated and shortened, and thus, the depreciation rates are greater than if the ALG procedure is used and/or maintained." Explain whether Mr. Kollen is asserting that Atmos Energy Corporation (Atmos) has used the ALG procedure to calculate depreciation rates in the past.
- d. Provide any potential issues that could occur if Atmos begins utilizing the ALG procedure instead of the ELG procedure to calculate depreciation rates.
- e. Describe Mr. Kollen's education, training, and experience as it relates to determining depreciation rates and procedures.

RESPONSE:

- a. Yes. Mr. Kollen recommends use of the ALG procedure over the ELG procedure in all instances for the reasons cited in his Direct Testimony. The natural gas utility will recover the entirety of its plant costs through depreciation expense under either the ELG procedure or the ALG

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procedure. The issue is one of timing. The ELG procedure provides accelerated recovery compared to the ALG procedure. The ELG procedure effectively compounds the rate effects on customers from new plant additions. The ELG depreciation rates and expense are at their peak and the return on rate base is at its peak when construction work in progress is closed to plant. In contrast, the ALG depreciation rates and expense are levelized over the service lives of all vintages of plant, which tends to mitigate the effects of new plant additions and ensures that all generations of customers provide a proportionate recovery, as opposed to a declining recovery, of all plant costs through depreciation expense over the entire service lives of all assets.

- b. See response to subpart a.
- c. Atmos has utilized the ELG procedure to compute depreciation rates since new depreciation rates were adopted in Case No. 1999-0070, according to the Company's response to AG 2-22 in Case No. 2017-00349. The Company's response to that request is as follows:

The earliest rate filing in which the Company is able to confirm the approval of depreciation rates calculated with the ELG procedure is Case No. 99-070. However, ELG depreciation rates could have been approved in prior filings.

The Order in Case No. 1999-0070 does not address depreciation, let alone the use of the ELG procedure to calculate the depreciation rates. The case was resolved through a settlement, which is not available on the Commission's website and Mr. Kollen has not been able to review it. It is possible that the Company filed for new depreciation rates using the ELG procedure, but the settlement may not specifically address it.

- d. Mr. Kollen does not know of any potential issues related to the utilization of the ALG procedure instead of the ELG procedure to determine depreciation rates other than the potential generational inequities due to

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the return of excessive depreciation taken in prior years over the remaining service lives of the assets rather than a shorter period.

- e. Mr. Kollen has an undergraduate degree in accounting, which included coursework on the calculation of depreciation expense under generally accepted accounting principles. In addition, Mr. Kollen has studied the NARUC depreciation manual. Further, Mr. Kollen has studied depreciation in conjunction with several dozen rate proceedings and worked closely with depreciation experts who own or license depreciation software used specifically in the utility industry, although Mr. Kollen's firm does not own or license depreciation software. Finally, Mr. Kollen has testified in at least two dozen proceedings over the last ten years on depreciation issues, including numerous proceedings before the Commission. Mr. Kollen has marked a copy of his Exhibit\_\_\_(LK-1) to note the proceedings in which he has testified on depreciation issues in the last ten years.

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Refer to the Kollen Testimony, pages 14-20. Confirm that Atmos could integrate a historic period pipeline replacement program (PRP) rider into an annually filed, forecasted-test-period rate case. If confirmed, discuss the appropriate methodology for determining rate base for base rates after the PRP rider is filed using a historic period, and discuss how PRP rider amounts would be rolled into base rates.

RESPONSE:

Confirmed. Mr. Kollen is not a lawyer and cannot provide a legal opinion in response to the question. Nevertheless, mechanically, the Commission could bifurcate the base revenue requirement into the PRP revenue requirement using a historic test year and the non-PRP revenue requirement using a forecast test year. Due to the problems with the PRP addressed by the Commission in prior proceedings and its decisions to resolve the problems in the last base rate proceeding, Mr. Kollen now believes that the Commission should maintain a separate PRP Rider so that it can focus on the Company's progress, or lack thereof, in the PRP miles and costs. The PRP Rider also ensures that the reductions in PRP rate base due to book and tax depreciation are timely reflected in customer rates regardless of the timing of the Company's base rate case filings. This will be an important consideration if and when the Company's PRP is ever completed, all else equal.

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Refer to the Kollen Testimony at pages 14-26, in which he discusses his proposed reductions to rate base arising from his reduction of PRP and Non-PRP capital expenditures.

- a. State whether Mr. Kollen contends that Atmos failed to establish that its projected PRP and Non-PRP investment costs would lead to fair, just, and reasonable rates.
- b. Identify and explain each basis for Mr. Kollen's contention that Atmos's projected PAP and Non-PAP investment costs, or any portions thereof, are unreasonable other than his assertion that the costs are inconsistent with the Commission's final Order in Case No. 2017-00349<sup>1</sup> and that the costs and projected costs have significantly increased since 2013.
- c. Assuming Atmos's projections are accurate, state whether Mr. Kollen contends that Atmos's projected PAP and Non-PAP investment costs or any portion thereof are unnecessary to provide adequate service or are inconsistent with the investment costs of similarly situated companies, and explain each basis for his contentions.

RESPONSE:

- a. Yes. The Company violated the Commission's specific direction for recovery of the PRP costs in Case No. 2017-00349, although it incorrectly claimed that it complied with those directions in its testimony in this proceeding. None of the PRP costs after September 2018 and forecast through the end of the test year are allowed recovery in the base revenue requirement in this proceeding unless the Commission terminates the PRP Rider and reverses and rejects the consumer safeguards that it ordered approximately a year ago in Case No. 2017-00349. In addition, Mr. Kollen contends that the forecast non-PRP capital expenditures are not reasonable compared to the Company's recent history of actual non-PRP capital expenditures.
- b,c. Mr. Kollen believes that the Commission must assess the reasonableness of forecast capital expenditures given no or minimal customer growth, prior Orders limiting recovery of PRP capital expenditures, and the

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<sup>1</sup> Case No. 2017-00349, Electronic Application of Atmos Energy Corporation for an Adjustment of Rates and Tariff Modifications, (Ky. PSC May 3, 2018).



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magnitude of the capital expenditures compared to history and the effect on customer rates. In every base rate proceeding, the Commission has the opportunity to retain or implement various behavioral incentives for the utility to control its capital expenditures and to avoid or reject behavioral incentives to increase capital expenditures. The Commission must balance the utility's inherent incentives to grow rate base against the effect on customers who necessarily must pay for this increase in rate base through increases in their rates. With respect to the non-PRP capital expenditures, the Commission must decide whether the forecast capital expenditures are reasonable. Atmos has the burden of proof. Atmos has not justified the extreme increases in non-PRP capital expenditures that it proposes. In fact, to the contrary, and as discussed by Mr. Kollen in his Direct Testimony, the Company has engaged in gamesmanship by claiming that it reduced PRP capital expenditures to "comply" with the Commission's Order in Case No. 2017-00349, but then increased its non-PRP forecast capital expenditures so that the total remains the same. This is hardly good faith and it is something that should not be afforded any presumption of reasonableness.

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Refer to the Kollen Testimony, page 26, lines 16-18. Explain whether this amount should be adjusted for inflation. If not, explain why not. If so, discuss whether a factor based on the consumer price index or the gross domestic product (GDP) deflater is more appropriate.

RESPONSE:

Mr. Kollen did not add an adjustment for inflation. The Commission previously ruled against the use of a “generic” inflation factor, such as the CPI, for forecasting increases in certain O&M expenses in Case No. 2013-00148. The Commission stated the following in its Order in the case:

While it has on occasion accepted inflation-related adjustments for individual expense items,<sup>44</sup> the Commission has not been, and is not now, inclined to accept an expense level based on application of a standard, or generic, inflation factor to a mix of approximately a dozen different cost categories ranging from Vehicles and Equipment to Travel and Entertainment. Commission orders in prior cases stated the Commission’s view on this type of CPI-based proposal by finding that using the CPI relies “...upon too large and diverse a group of goods and services.” In its decision involving the water rates of the city of Lawrenceburg, the Commission also stated that the adjustment proposal “... must provide an accurate measurement of changes in the cost of providing water service. It therefore should be based principally on those goods and services that are reasonably likely to be used to provide water service.”<sup>45</sup> The Commission reasoned that a proper adjustment “... should reflect all changes in the cost of the inputs that are required to provide water service” (emphasis in original) and that reliance on the CPI would “... not reflect any reductions in the cost of service, only increases.”<sup>46</sup>

Finding no persuasive reason to depart from its previous decisions on the reasonableness of basing cost increases on a generic inflation factor, the Commission denies Atmos-Ky.’s proposal.<sup>47</sup> With the corrections to the AG’s adjustment provided in Atmos-Ky.’s rebuttal, the result is a \$171,804 reduction in test-year operating expenses.

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Refer to the Kollen Testimony, page 34, lines 9-13, and page 35, lines 19-20. Provide the methodology for removing the previously accrued allowance for funds used during construction (AFUDC) from rate base.

RESPONSE:

Plant in rate base includes AFUDC that the Company has recorded over many years. If the Company has sufficiently detailed records, it should be directed to quantify the AFUDC included in plant additions and retirements for each plant account in each prior year and calculate the related accumulated depreciation and accumulated deferred income taxes for the base period and test year in this and future rate proceedings. The net of these amounts would be removed from rate base.

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Refer to the Kollen Testimony, pages 36-38.

- a. Provide the case number of any case in which the Commission has removed non-cash items from a lead/lag study or accepted a lead/lag study in which noncash items were removed.
- b. Explain in detail how a negative \$5.503 million cash-working capital is reasonable.
- c. Provide any case that Mr. Kollen is aware of in which a utility has a negative cash-working capital.

RESPONSE:

- a. Mr. Kollen has not reviewed all other Kentucky cases to know if, or if so, how, the Commission has removed non-cash items in any of those cases. Mr. Kollen is familiar only with recent cases in which the utility filed a cash working capital study using the lead/lag approach and did not remove the non-cash expenses or include all cash expenses, both of which are errors.
- b. A negative cash working capital simply means that the Company's customers provide capital, on a net basis, for the leads and lags on cash inflows and disbursements related to operating revenues and expenses. The result of a correctly performed cash working capital using the lead/lag approach necessarily is reasonable if the methodology, assumptions, and calculations are reasonable.
- c. In Mr. Kollen's experience, nearly all utilities have negative cash working capital if the lead/lag approach is correctly performed. An example of this is found in lead/lag studies filed in other Atmos division proceedings. As cited in Mr. Kollen's Direct Testimony in Case No. 2017-00349 at pages 32-34, including footnote 26, Atmos has a number of divisions in which the cash working capital calculations were filed as negative in recent years. The same cases were cited in Mr. Kollen's Direct Testimony in Case No. 2015-00343 and copies of Atmos's filings were provided as Exhibit\_\_(LK-14). In Colorado Docket No. 13AL-0496G (2012), Atmos filed a working capital analysis with \$77.668 million in operating expenses

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and negative \$2.773 million cash working capital. In Colorado Docket No. 14AL-0300G (2013), Atmos filed a working capital analysis with \$103.090 million in operating expenses and negative \$3.836 million in cash working capital. In Colorado Docket No. 15AL-0299G (2014), Atmos filed a working capital analysis with \$105.723 million in operating expenses and negative \$2.578 million in cash working capital. In Texas Docket No. 10174 (2012), Atmos Mid-Tex filed a working capital analysis with \$179.219 million in operating expenses and negative \$1.957 million in cash working capital. In a Statement of Intent in Texas (2013), Atmos Mid-Tex filed a working capital analysis with \$173.655 million in operating expenses and negative \$2.757 million in cash working capital. In Virginia Docket No. PUE-2015-00119, Atmos Virginia filed a working capital analysis with negative \$0.168 million in cash working capital, although that study erroneously included amounts for non-cash depreciation and deferred income taxes. When these amounts are removed, the study reflects negative \$0.358 million in cash working capital.

While Mr. Kollen has not performed a detailed study of all utilities in all states in order to respond to this request, he is aware of numerous negative cash working capital amounts pertaining to regulated utilities in Texas due to provisions found in Texas Substantive Rule §25.231(c)(2)(B)(iii) requiring removal of all non-cash items. A few provisions of that rule state the following:

(IV) For all investor-owned electric utilities a reasonable allowance for cash working capital, including a request of zero, will be determined by the use of a lead-lag study. A lead-lag study will be performed in accordance with the following criteria:

(-a-) The lead-lag study will use the cash method; all non-cash items, including but not limited to depreciation, amortization, deferred taxes, prepaid items, and return (including interest on long-term debt and dividends on preferred stock), will not be considered.

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...

(-g-) If the cash working capital calculation results in a negative amount, the negative amount shall be included in rate base.

(V) If cash working capital is required to be determined by the use of a lead-lag study under the previous subclause and either the electric utility does not file a lead lag study or the electric utility's lead-lag study is determined to be so flawed as to be unreliable, in the absence of persuasive evidence that suggests a different amount of cash working capital, an amount of cash working capital equal to negative one-eighth of operations and maintenance expense including fuel and purchased power will be presumed to be the reasonable level of cash working capital.

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Lane Kollen

QUESTION No. 7

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Refer to the Kollen Testimony, page 38, line 20. Explain how the dividend component of the return on equity was calculated.

RESPONSE:

Refer to the formula contained in cell E51 of the worksheet "As Adjusted ATO-CWC1A" in the electronic revenue requirement workpaper filed with Mr. Kollen's Direct Testimony. That formula multiplies the Company's requested rate base times the Company's requested common equity percentage of the total capital structure times 3%, the dividend yield component of Dr. Vander Weide's return on equity DCF calculations. These amounts can be synchronized when all other components of the case affecting the balances of cash working capital are determined.

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Lane Kollen

QUESTION No. 8

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Refer to the Kollen Testimony, page 41, lines 7-10. Explain whether the recommendation to "cap the common equity" applies only to this proceeding.

RESPONSE:

No. It also would apply to future PRP Rider filings if the Commission rejects the Company's proposal to terminate the PRP Rider. Mr. Kollen may make a similar recommendation in a future base rate proceeding if retained by the AG to address this issue.



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Lane Kollen

QUESTION No. 9

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Refer to the Kollen Testimony, page 44, lines 15-18.

- a. Confirm that the debt issuance will likely occur before the public hearing in this proceeding. If confirmed, explain why the actual Treasury yield component of the debt issuance should not be utilized.
- b. Explain whether Atmos's proposed credit spread of 1.0 percent is reasonable.

RESPONSE:

- a. Confirmed, assuming that Atmos actually issues the new debt on or before the forecast issuance date of March 15, 2019. If the actual interest rate is available before the public hearing, then the Commission could use that rate.
- b. Mr. Kollen did not assess whether the credit spread was reasonable. He simply accepted it for purposes of this case.

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Lane Kollen

QUESTION No. 10

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Refer to the Kollen Testimony, page 47, lines 1-3. Provide all updates to the average actual authorized return on equity in general gas rate cases from January 2018 through December 2018, if available, and all supporting documentation regarding the same.

RESPONSE:

As stated in footnote 37 at page 47 of Mr. Kollen's Direct Testimony, the data relied upon was sourced from a discovery response provided by Kentucky Utilities Company in Case No. 2018-00294. Mr. Kollen will provide any updates that become available to him and that are not confidential or otherwise protected.

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Lane Kollen

QUESTION No. 11

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Refer to the Kollen Testimony, pages 48-50.

- a. Identify any changes, excluding updates to the composite factors and revenue requirement impact, from Case No. 2017-00349, the Direct Testimony of Mr. Kollen, pages 63-65.
- b. Confirm that Atmos has allocated costs in accordance with its cost allocation manual.

RESPONSE:

- a. Mr. Kollen does not understand the question with the reference to Case No. 2017-00349. Notwithstanding, Mr. Kollen states that his recommendation in this case is consistent with his recommendation from Case No. 2017-00349 in terms of methodology. The Commission did not address Mr. Kollen's recommendation regarding the appropriate composite factor in its Order in that case.
- b. Mr. Kollen understands that Atmos has allocated costs in accordance with its cost allocation manual.

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Lane Kollen

QUESTION No. 12

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Refer to the Kollen Testimony, pages 49-50. Confirm that using total operating expenses as a component of the composite factor produces circular results in that allocated costs are included in total operating expenses. If this cannot be confirmed, provide a detailed explanation.

RESPONSE:

Mr. Kollen relied on Attachment 3 to the Company's response to AG1-31. This response provides "Total Direct Operating Expenses," which do not include allocated costs.

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Lane Kollen

QUESTION No. 13

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Refer to the Federal Energy Regulatory Commission (FERC) order issued on April 27, 2018, in the matter involving Midcontinent Independent System Operator, Inc., and others in which FERC determined that the "two-step averaging methodology" used to calculate accumulated deferred income tax (ADIT) in a future test period for ratemaking purposes resulted in unfair and unreasonable rates,<sup>2</sup> and refer to Atmos's response to Staff's Second Request, Item 70.

- a. State whether Mr. Kollen has an opinion as to whether the "two-step averaging methodology" is required by normalization rules.
- b. If so, provide his opinion and explain each basis for the same.

RESPONSE:

(a. and b.)

Mr. Kollen has not reviewed the referenced FERC decision, applicable private letter rulings, and case history in enough detail to form an opinion in this matter.

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<sup>2</sup> *In Re Midcontinent Independent System Operator, Inc., et. al.*, 163 FERC P 61, 061, 2018 WL 2017529 (F.E.R.C. April 27, 2018).

**AFFIDAVIT**

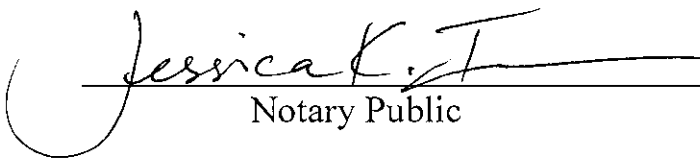
STATE OF GEORGIA        )

COUNTY OF FULTON        )

LANE KOLLEN, being duly sworn, deposes and states: that the attached is his sworn testimony and that the statements contained are true and correct to the best of his knowledge, information and belief.

  
Lane Kollen

Sworn to and subscribed before me on this  
27th day of February 2019.

  
Notary Public

