COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF KENTUCKY-AMERICAN WATER COMPANY FOR AN ADJUSTMENT OF RATES	))))	CASE NO. 2018-00358

ATTORNEY GENERAL AND LEXINGTON-FAYETTE URBAN COUNTY GOVERNMENT'S RESPONSES TO DATA REQUESTS FROM THE KENTUCKY PUBLIC SERVICE COMMISSION STAFF

Comes now the intervenors, the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention ("Attorney General"), and Lexington-Fayette Urban County Government ("LFUCG"), by and through counsel, submits the following responses to data requests from the Kentucky Public Service Commission Staff ("Staff") in the above-styled matter.

Respectfully submitted,

ANDY BESHEAR
ATTORNEY GENERAL

Justin McNeil

____

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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
12th day of April 2019.

Notary Public

RANDY A. FUTRAL
MY COMMISSION EXPIRES
NOTARY
PUBLIC
AUGUST 26, 2020
COBB COUNTY, GEORGIA

AFFIDAVIT

STATE OF GEORGIA)

COUNTY OF FULTON)

RICHARD A. BAUDINO, 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.

Richard A. Baudino

Sworn to and subscribed before me on this
12th day of April 2019.

Notary Public

RANDY A. FUTRAL
MY COMMISSION EXPIRES
NOTARY PUBLIC
AUGUST 26, 2020
COBB COUNTY, GEORGIA

WITNESS/RESPONDENT RESPONSIBLE:
Lane Kollen
Page 1 of 1

QUESTION No. 1

Refer to the Direct Testimony of Lane Kollen (Kollen Testimony), page 7, lines 5–8, regarding American Water Works Service Company, Inc.'s (AWWS) practice of invoicing Kentucky-American Water Company (Kentucky-American) for the estimated expenses for the current month plus or minus a true-up for the prior month. Mr. Kollen states that it is unusual for a service company to invoice for estimated expenses.

a. Identify any other utilities that Mr. Kollen is aware of that invoice for estimated expenses at the beginning of the month.

b. Explain whether AWWS bills an estimated expense to all of its affiliates.

RESPONSE:

a. Mr. Kollen is not aware of any other service company that bills its affiliate utilities for estimated expenses subject to a true up.

b. Mr. Kollen does not know whether AWWS bills its other affiliates for estimated expenses.

WITNESS/RESPONDENT RESPONSIBLE:
Lane Kollen
Page 1 of 1

QUESTION No. 2

Refer to the Kollen Testimony, page 19, lines 17–19. Mr. Kollen proposes to defer lost revenues associated with the closing of the Trane Lexington plant as a regulatory liability and amortize them over two years.

a. Explain why two years was chosen.

b. Provide an explanation supporting the proposed amortization of this lost revenue.

RESPONSE:

a., b. Mr. Kollen recommends a two-year amortization period based on the small magnitude of the lost revenues. The two-year period is only one year less than the three-year amortization period proposed by the Company for rate case expenses, which are much larger in magnitude. Furthermore, the schedule in which KAW has historically filed rate cases supports the use of a two-year amortization.

WITNESS/RESPONDENT RESPONSIBLE:
Lane Kollen
Page 1 of 1

QUESTION No. 3

Refer to the Kollen Testimony, page 29, lines 9–10, which states that an adjustment disallowing the retirement plan expense incurred for employees who participate in both defined benefit and defined contribution retirement plans would reduce the retirement plan expense by $0.070 million and reduce the revenue requirement of $0.071 million. Provide a schedule in Excel spreadsheet format, with all formulas intact and unprotected and all rows and columns accessible, that supports your calculation of the reduction, and include a breakdown of the total reduction in the retirement plan expense detailing the amounts for hourly union employees, hourly non-union employees, and exempt employees.

RESPONSE:

Mr. Kollen utilized the data provided by the Company in the referenced response to AG 1-10, which he replicated as Exhibit___(LK-14). The Company did not provide the data in live Excel format or in the format requested. Mr. Kollen used the following amounts from the response for his quantifications.

Test Year Expense for KAW Employees		$38,433
(Response to AG 1-10 (Public), Page 2 of 13)		
Test Year Expense Allocated to KAW - AWWS Employees		$31,550
(Response to AG 1-10 (Public), Page 13 of 13)		
Total Test Year Expense		$69,983
Bad Debt and PSC Gross-up	x	1.01127
Total Test Year Revenue Requirement		$70,772

WITNESS/RESPONDENT RESPONSIBLE:
Lane Kollen
Page 1 of 1

QUESTION No. 4

Refer to the Kollen Testimony, page 37, line 19 to page 38, line 3, regarding excess Accumulated Deferred Income Taxes (ADIT) due to the repair allowance.

a. Provide the basis for Mr. Kollen's proposal to amortize the unprotected excess Accumulated Deferred Income Taxes (ADIT) over three years.

b. Explain whether the average amortization life of the unprotected excess ADIT should be used rather than the proposed three-year amortization period.

RESPONSE:

a. Mr. Kollen recommends the same three-year amortization period for the "unprotected" excess ADIT that the Company requests for rate case expenses. The Company's request for a three-year amortization period is based on its estimate of the number of years until its rates are reset in its next base rate case. The Commission has complete discretion as to the amortization period for unprotected excess ADIT. The objective is to refund the amounts that were collected from customers in prior years in a reasonably short period of time to match the customers who paid these taxes as closely as possible.

b. No. There no longer is a relationship between the underlying temporary differences and the excess ADIT regardless of whether it is unprotected or protected, except for the requirements imposed by the TCJA for the protected amounts. These are now regulatory liabilities for the refunds due to customers and should be returned to customers as soon as possible, subject to the limitations imposed by the TCJA for the protected amounts.

WITNESS/RESPONDENT RESPONSIBLE:
Richard Baudino
Page 1 of 1

QUESTION No. 5

Refer to the Direct Testimony of Richard A. Baudino (Baudino Testimony), page 9, lines 22–25 and page 10, line 1. Provide any updates to these projections based on the March 20, 2019 Federal Open Market Committee (FOMC) Meeting.

RESPONSE:

Please refer to the attached update of the Federal Reserve's economic projections dated March 20, 2019. With respect to the data cited by Mr. Baudino, the updated numbers are:

- Projected federal funds rate of 2.4% for 2019, 2.6% for 2020, 2.6% for 2021, and 2.8% for the longer run.
- Inflation rate of 2.0% for 2019 - 2021 and the longer run.

Economic projections of Federal Reserve Board members and Federal Reserve Bank presidents under their individual assessments of projected appropriate monetary policy, March 2019

Advance release of table 1 of the Summary of Economic Projections to be released with the FOMC minutes

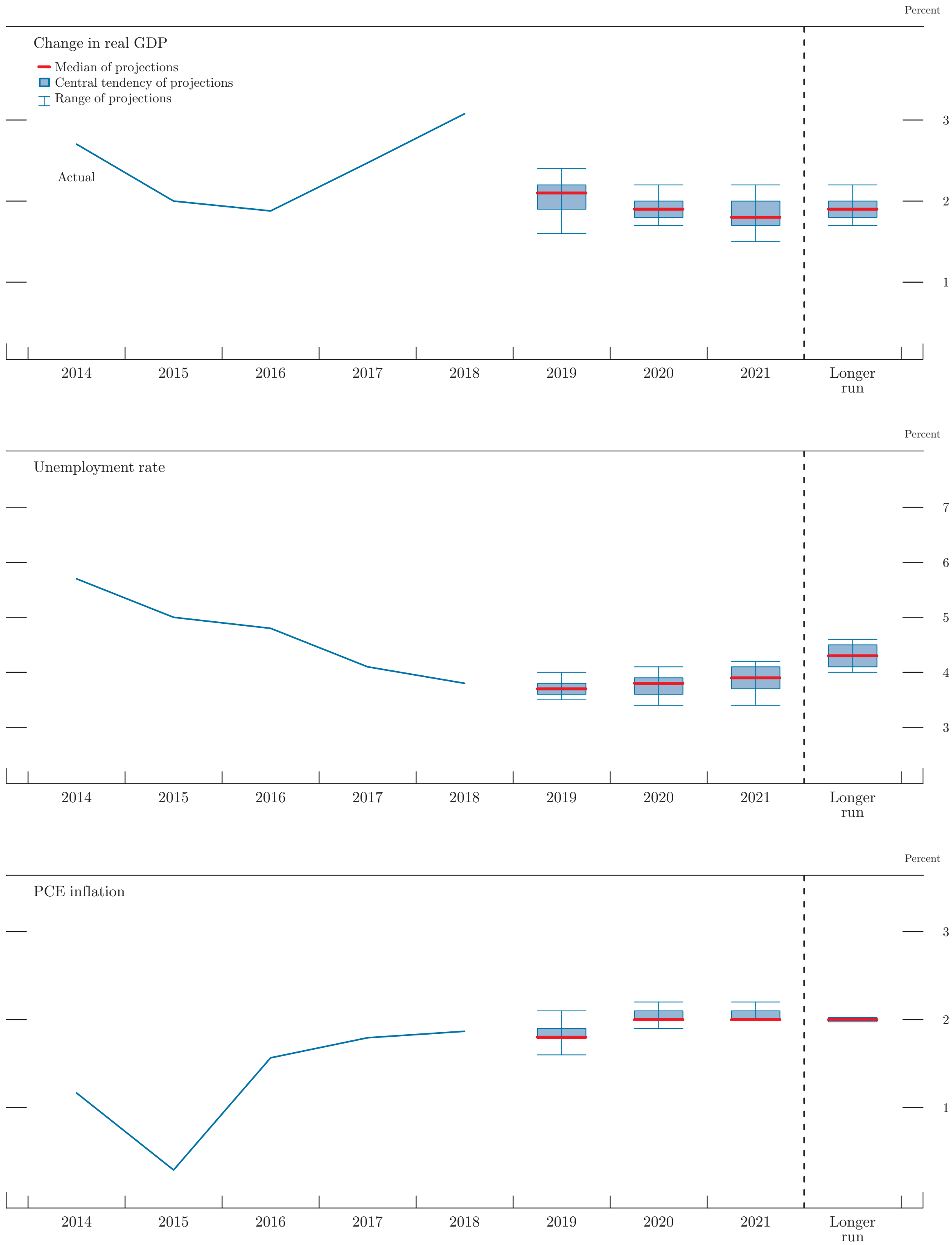
Percent

Variable	Median[1]				Central tendency[2]				Range[3]			
	2019	2020	2021	Longer run	2019	2020	2021	Longer run	2019	2020	2021	Longer run
Change in real GDP	2.1	1.9	1.8	1.9	1.9 – 2.2	1.8 – 2.0	1.7 – 2.0	1.8 – 2.0	1.6 – 2.4	1.7 – 2.2	1.5 – 2.2	1.7 – 2.2
December projection	2.3	2.0	1.8	1.9	2.3 – 2.5	1.8 – 2.0	1.5 – 2.0	1.8 – 2.0	2.0 – 2.7	1.5 – 2.2	1.4 – 2.1	1.7 – 2.2
Unemployment rate	3.7	3.8	3.9	4.3	3.6 – 3.8	3.6 – 3.9	3.7 – 4.1	4.1 – 4.5	3.5 – 4.0	3.4 – 4.1	3.4 – 4.2	4.0 – 4.6
December projection	3.5	3.6	3.8	4.4	3.5 – 3.7	3.5 – 3.8	3.6 – 3.9	4.2 – 4.5	3.4 – 4.0	3.4 – 4.3	3.4 – 4.2	4.0 – 4.6
PCE inflation	1.8	2.0	2.0	2.0	1.8 – 1.9	2.0 – 2.1	2.0 – 2.1	2.0	1.6 – 2.1	1.9 – 2.2	2.0 – 2.2	2.0
December projection	1.9	2.1	2.1	2.0	1.8 – 2.1	2.0 – 2.1	2.0 – 2.1	2.0	1.8 – 2.2	2.0 – 2.2	2.0 – 2.3	2.0
Core PCE inflation[4]	2.0	2.0	2.0		1.9 – 2.0	2.0 – 2.1	2.0 – 2.1		1.8 – 2.2	1.8 – 2.2	1.9 – 2.2	
December projection	2.0	2.0	2.0		2.0 – 2.1	2.0 – 2.1	2.0 – 2.1		1.9 – 2.2	2.0 – 2.2	2.0 – 2.3	
Memo: Projected appropriate policy path												
Federal funds rate	2.4	2.6	2.6	2.8	2.4 – 2.6	2.4 – 2.9	2.4 – 2.9	2.5 – 3.0	2.4 – 2.9	2.4 – 3.4	2.4 – 3.6	2.5 – 3.5
December projection	2.9	3.1	3.1	2.8	2.6 – 3.1	2.9 – 3.4	2.6 – 3.1	2.5 – 3.0	2.4 – 3.1	2.4 – 3.6	2.4 – 3.6	2.5 – 3.5

Note: Projections of change in real gross domestic product (GDP) and projections for both measures of inflation are percent changes from the fourth quarter of the previous year to the fourth quarter of the year indicated. PCE inflation and core PCE inflation are the percentage rates of change in, respectively, the price index for personal consumption expenditures (PCE) and the price index for PCE excluding food and energy. Projections for the unemployment rate are for the average civilian unemployment rate in the fourth quarter of the year indicated. Each participant's projections are based on his or her assessment of appropriate monetary policy. Longer-run projections represent each participant's assessment of the rate to which each variable would be expected to converge under appropriate monetary policy and in the absence of further shocks to the economy. The projections for the federal funds rate are the value of the midpoint of the projected appropriate target range for the federal funds rate or the projected appropriate target level for the federal funds rate at the end of the specified calendar year or over the longer run. The December projections were made in conjunction with the meeting of the Federal Open Market Committee on December 18–19, 2018. One participant did not submit longer-run projections for the change in real GDP, the unemployment rate, or the federal funds rate in conjunction with the December 18–19, 2018, meeting, and one participant did not submit such projections in conjunction with the March 19–20, 2019, meeting.

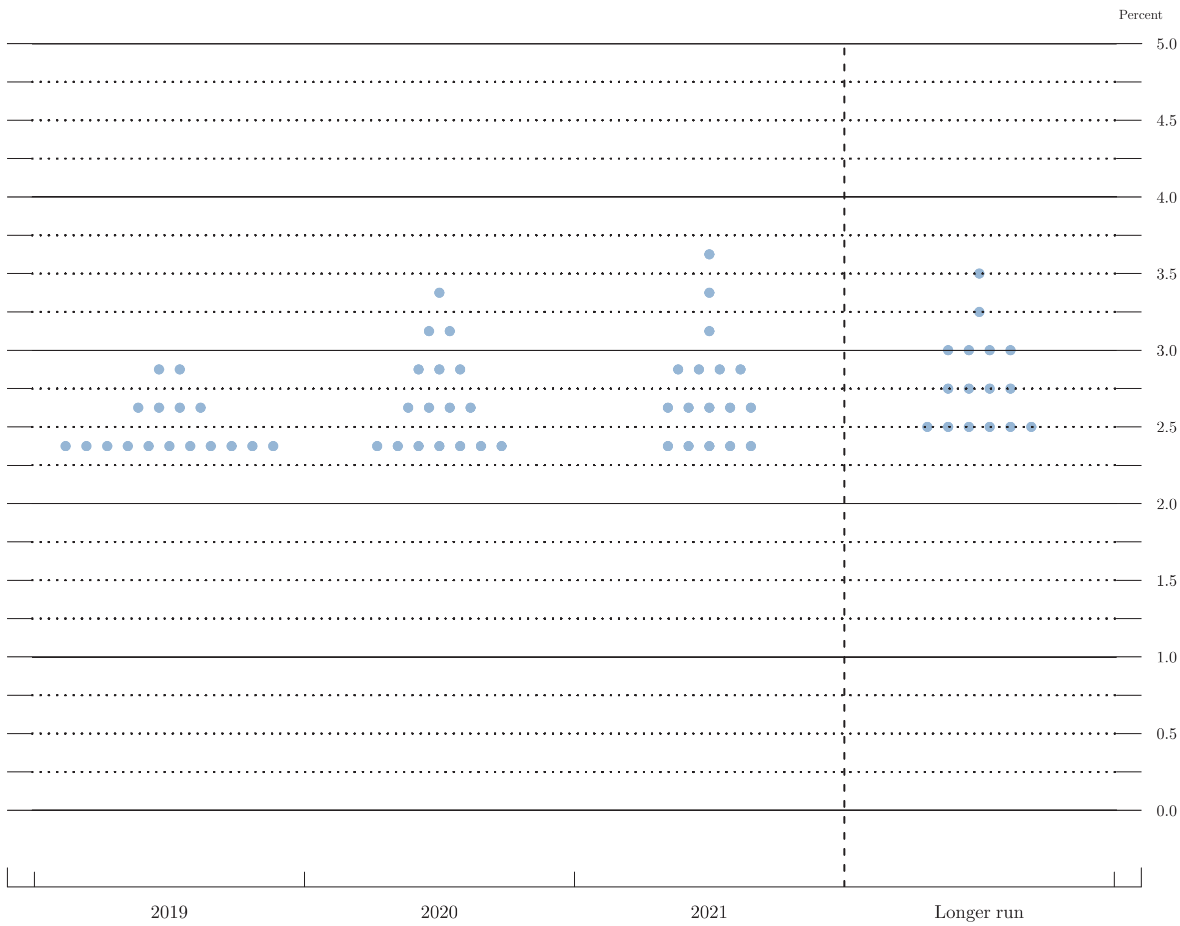
1. For each period, the median is the middle projection when the projections are arranged from lowest to highest. When the number of projections is even, the median is the average of the two middle projections.
2. The central tendency excludes the three highest and three lowest projections for each variable in each year.
3. The range for a variable in a given year includes all participants' projections, from lowest to highest, for that variable in that year.
4. Longer-run projections for core PCE inflation are not collected.

Figure 1. Medians, central tendencies, and ranges of economic projections, 2019–21 and over the longer run



Note: Definitions of variables and other explanations are in the notes to the projections table. The data for the actual values of the variables are annual.

Figure 2. FOMC participants' assessments of appropriate monetary policy: Midpoint of target range or target level for the federal funds rate



Note: Each shaded circle indicates the value (rounded to the nearest 1/8 percentage point) of an individual participant's judgment of the midpoint of the appropriate target range for the federal funds rate or the appropriate target level for the federal funds rate at the end of the specified calendar year or over the longer run. One participant did not submit longer-run projections for the federal funds rate.

Explanation of Economic Projections Charts

The charts show actual values and projections for three economic variables, based on FOMC participants' individual assessments of appropriate monetary policy:

- Change in Real Gross Domestic Product (GDP)—as measured from the fourth quarter of the previous year to the fourth quarter of the year indicated.
- Unemployment Rate—the average civilian unemployment rate in the fourth quarter of each year.
- PCE Inflation—as measured by the change in the personal consumption expenditures (PCE) price index from the fourth quarter of the previous year to the fourth quarter of the year indicated.

Information for these variables is shown for each year from 2014 to 2021, and for the longer run.

The solid blue line, labeled "Actual," shows the historical values for each variable.

The solid red lines depict the median projection in each period for each variable. The median value in each period is the middle projection when the projections are arranged from lowest to highest. When the number of projections is even, the median is the average of the two middle projections.

The range and central tendency for each variable in each projection period are depicted in "box and whiskers" format. The blue connected horizontal and vertical lines ("whiskers") represent the range of the projections of policymakers. The bottom of the range for each variable is the lowest of all of the projections for that year or period. Likewise, the top of the range is the highest of all of the projections for that year or period. The light blue shaded boxes represent the central tendency, which is a narrower version of the range that excludes the three highest and three lowest projections for each variable in each year or period.

The longer-run projections, which are shown on the far right side of the charts, are the rates of growth, unemployment, and inflation to which a policymaker expects the economy to converge over time—maybe in five or six years—in the absence of further shocks and under appropriate monetary policy. Because appropriate monetary policy, by definition, is aimed at achieving the Federal Reserve's dual mandate of maximum employment and price stability in the longer run, policymakers' longer-run projections for economic growth and unemployment may be interpreted, respectively, as estimates of the economy's normal or trend rate of growth and its normal unemployment rate over the longer run. The longer-run projection shown for inflation is the rate of inflation judged to be most consistent with the Federal Reserve's dual mandate.

For release at 2:00 p.m., EDT, March 20, 2019

Explanation of Policy Path Chart

This chart is based on policymakers' assessments of appropriate monetary policy, which, by definition, is the future path of policy that each participant deems most likely to foster outcomes for economic activity and inflation that best satisfy his or her interpretation of the Federal Reserve's dual objectives of maximum employment and stable prices.

Each shaded circle indicates the value (rounded to the nearest ⅛ percentage point) of an individual participant's judgment of the midpoint of the appropriate target range for the federal funds rate or the appropriate target level for the federal funds rate at the end of the specified calendar year or over the longer run.

WITNESS/RESPONDENT RESPONSIBLE:
Richard Baudino
Page 1 of 1

QUESTION No. 6

Refer to the Baudino Testimony, page 12. Provide an update to Table 1 with March data.

RESPONSE:

Please refer to the attached update of Table 1.

TABLE 1
Bond Yields and DJUA

	Federal Funds Rate %	30-Year Treasury %	Avg. Utility Bond %	DJUA
2016				
January	0.34	2.86	4.62	611.35
February	0.38	2.62	4.44	620.70
March	0.36	2.68	4.40	668.57
April	0.37	2.62	4.16	654.44
May	0.37	2.63	4.06	659.44
June	0.38	2.45	3.93	716.52
July	0.39	2.23	3.70	711.42
August	0.40	2.26	3.73	666.87
September	0.40	2.35	3.80	668.13
October	0.40	2.50	3.90	675.23
November	0.41	2.86	4.21	632.67
December	0.54	3.11	4.39	645.86
2017				
January	0.65	3.02	4.24	668.87
February	0.66	3.03	4.25	703.16
March	0.79	3.08	4.30	697.28
April	0.90	2.94	4.19	704.35
May	0.91	2.96	4.19	726.62
June	1.04	2.80	4.01	706.91
July	1.15	2.88	4.06	726.48
August	1.16	2.80	3.92	743.24
September	1.15	2.78	3.93	723.60
October	1.15	2.88	3.97	753.20
November	1.16	2.80	3.88	770.39
December	1.30	2.77	3.85	723.37
2018				
January	1.41	2.88	3.91	699.25
February	1.42	3.13	4.15	668.81
March	1.51	3.09	4.21	692.63
April	1.69	3.07	4.24	707.01
May	1.70	3.13	4.36	695.21
June	1.82	3.05	4.37	711.64
July	1.91	3.01	4.38	724.24
August	1.91	3.04	4.33	726.41
September	1.95	3.15	4.41	720.60
October	2.19	3.34	4.56	733.84
November	2.20	3.36	4.65	741.92
December	2.27	3.10	4.51	712.93
2019				
January	2.40	3.04	4.48	727.25
February	2.40	3.02	4.35	756.34
March	2.41	2.98	4.26	778.72

Source: Federal Reserve, Mergent Bond Record, Yahoo! Finance

WITNESS/RESPONDENT RESPONSIBLE:
Richard Baudino
Page 1 of 1

QUESTION No. 7

Refer to the Baudino Testimony, page 32, line 7. The market return portion of the Capital Asset Pricing Model (CAPM) is estimated to be 12.16 percent. The market return estimated by Kentucky-American's expert, Ann E. Bulkley, is 15.19 percent, over 300 basis points larger. Provide an explanation discussing the key differences in modeling the market return and why the two models differ to such a degree.

RESPONSE:

The key difference between Ms. Bulkley and Mr. Baudino in terms of modeling the market return is the source of the data used to estimate that return. Ms. Bulkley used a DCF model to estimate a return on the Standard and Poor's 500 companies. Her version of the model employed forecasted growth rates for each company from Bloomberg Professional. The average expected long-term growth rate shown on page 1 of Attachment AEB-8 is 13.18%, leading to the 15.19%.

As Mr. Baudino explained in his Direct Testimony on page 32, he used the Value Line Investment Survey to estimate two different estimated returns on the market. One estimate was Value Line's projected 3-5 year total return, which included 1,675 companies. This proxy for the market return was 13%, slightly lower than the growth rate for earnings used by Ms. Bulkley. The second market return estimate was calculated using the DCF model with earnings and book value growth averaged for the expected growth rate. The resulting market return from that method was 11.32%. Averaging the two alternative market return estimates resulted in the 12.16% number Mr. Baudino used in his CAPM analyses.

WITNESS/RESPONDENT RESPONSIBLE:
Richard Baudino
Page 1 of 1

QUESTION No. 8

Refer to the Baudino Testimony, page 59, lines 16–23. Mr. Baudino recommends a yearly and cumulative rate cap of 2.5 percent for the proposed QIP stating that this is a reasonable yearly increase.

a. Explain why 2.5 percent was chosen.

b. Provide any studies that support a yearly and communicative cap.

RESPONSE:

a., b. It is Mr. Baudino's view that 2.5% is a reasonable increase in that it is slightly greater than the current rate of inflation, which is approximately 2.0%, and strikes a reasonable balance between yearly rate increases to the Company's ratepayers and additional revenues for main replacement on the Company's system. Mr. Baudino did not base these recommendations on studies that he performed. Although his recommendation is not based on any studies he performed, the Commission has previously capped a utility's Pipeline Replacement Program to a specific dollar amount based on historical and expected spending.

WITNESS/RESPONDENT RESPONSIBLE:
Richard Baudino
Page 1 of 1

QUESTION No. 9

Refer to the Baudino Testimony, page 61, lines 11–17. Provide an outline of the QIP review process you would recommend the Commission implement and an estimate of a reasonable review period.

RESPONSE:

Mr. Baudino is not recommending the Commission adopt a QIP, and thus is not recommending a QIP review process. Mr. Baudino's discussion regarding a possible process was provided as an additional point for the Commission to consider only if it were to approve a QIP over the objections of the intervenors. To provide a specific process relating solely to KAW's proposed QIP, Mr. Baudino would need more information as to the scope of investments included in the QIP and whether the QIP would allow investment costs on an historical or forecasted basis. If, over the strenuous objections of the intervenors, the Commission approves some form of QIP in this proceeding, it should not provide KAW *carte blanche* to create the QIP in whatever form it chooses, without Commission and stakeholder direction.

WITNESS/RESPONDENT RESPONSIBLE:
Richard Baudino / Counsel as to Objection
Page 1 of 1

QUESTION No. 10

Refer to the Baudino Testimony, page 19, lines 19–23. It is proposed that the QIP be limited to a 2-year pilot program. State whether the Attorney General would support the QIP as a pilot program until Kentucky-American files its next base rate case.

RESPONSE:

Objection. The Attorney General has not provided testimony in this matter, and as counsel, is not prepared to individually respond to data requests in this matter. Notwithstanding this objection, counsel for both the Attorney General and LFUCG have indicated to Mr. Baudino that they intend to strenuously object to the QIP and will recommend that the Commission reject the proposal. Further, both parties have indicated they do not support a pilot program for the QIP.

WITNESS/RESPONDENT RESPONSIBLE:
Richard Baudino
Page 1 of 1

QUESTION No. 11

At the March 20, 2019 FOMC Meeting, the Federal Reserve (FED) maintained the target range for the federal funds rate at 2.25 percent and 2.50 percent and softened its economic outlook from the December FOMC meeting. Explain whether these announcements alter Mr. Baudino's proposed ROE of 9.15 percent.

RESPONSE:

This recent announcement by the Fed does not alter Mr. Baudino's recommendation and, in fact, supports Mr. Baudino's recommended ROE of 9.15%.

WITNESS/RESPONDENT RESPONSIBLE:
Richard Baudino / Counsel as to Objection
Page 1 of 1

QUESTION No. 12

Refer to the combined utility proxy group. Explain whether the Attorney General believes the inclusion of American Water Works is circular or not.

RESPONSE:

Objection. The Attorney General has not provided testimony in this matter, and as counsel, is not prepared to individually respond to data requests in this matter. Notwithstanding this objection, Mr. Baudino does not believe that the inclusion of American Water Works is circular. Further, given the small number of regulated water utilities available for inclusion in a proxy group, it is reasonable to include American Water Works.

WITNESS/RESPONDENT RESPONSIBLE:
Richard Baudino
Page 1 of 1

QUESTION No. 13

Refer to the Baudino Testimony. Provide all exhibits in Excel spreadsheet format with all formulas intact and unprotected and all rows and columns accessible.

RESPONSE:

Please refer to the attached Excel spreadsheet.