

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of

Electronic Application of Bluegrass Water)
Utility Operating Company, LLC for an)
Adjustment of Rates and Approval of)
Construction)

Case No. 2020-00290

**Response to
Joint Intervenors' Supplemental Data Requests**

Applicant Bluegrass Water Utility Operating Company, LLC (hereinafter "Bluegrass"), herewith submits its response to the Joint Intervenors' Supplemental Data Requests. A signed, notarized verification for this Response appears on the following page. The undersigned counsel is responsible for any objection noted for a particular response.

Respectfully Submitted,

/s/ Kathryn A. Eckert

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Company*

VERIFICATION

STATE OF MISSOURI)
)
COUNTY OF ST. LOUIS)

I, Mike Duncan, Vice President of Central States Water Resources, Inc., the manager of Applicant Bluegrass Water Utility Operating Company, LLC being duly sworn, state that I prepared or supervised the preparation of the following responses to Joint Intervenors' Supplemental Data Requests, and that the matters and things set forth in the responses are true and correct to the best of my knowledge, information and belief formed after reasonable inquiry.


Mike Duncan

Subscribed and sworn to this 18th day of March 2021, before me a Notary Public in and before said County and State.


Notary Public



MERANDA K. KEUBLER
My Commission Expires
November 13, 2022
St. Louis County
Commission #14631487

(SEAL)

My Commission expires: 11/13/2022

Request

1. Refer to your response to Staff DR-02-002. Please provide a copy of any depreciation study that was used to develop the depreciation rates upon which Bluegrass's depreciation rates are based.
-

Response

No depreciation study was used to develop Bluegrass Water's proposed depreciation rates.

Request

2. Refer to the letter to Mr. Wes Dement that begins on page five (5) of forty (40) of Bluegrass's Attachment 2-PSC-03. Please provide a copy of the referenced "status report detailing improvements and whether process changes are required" for the LH system.
-

Response

Please see the Excel workbook/spreadsheet titled "2-PSC-03_January2021-KY-SystemStatus.xlsx" listed at the end of the 2 PSC 03 response and provided as part of Bluegrass Water's responses to the Staff's Second Request for Information.

Request

3. Refer to Bluegrass's "January 2021 KY System Status.xlsx." Explain why there are no entries for Arcadia Pines, Carriage Park, Marshall Ridge and Randview.
-

Response

This update was prepared at the request of the EEC for the systems under Agreed Orders with the EEC/DEP. The four systems referenced in the request are not included in the agreed orders and therefore would not have been included in this update.

Request

4. Confirm whether Bluegrass seeks to capitalize its recovery of Construction Design and Investigative services expense.
-

Response

Bluegrass Water intends to capitalize and seek recovery of Construction Design and Investigative services expense.

Request

5. Refer to Bluegrass's ConstructionDesign_and_InvestigativeServicesCostsSummary.xlsx":
- a. Please confirm whether any of the work was performed by a company that is an affiliate or under common ownership with Bluegrass.
 - b. Please confirm how the firms providing the services were selected and retained.
 - c. Please describe the purpose of the work labeled as "surveying."
 - d. Please describe the nature of expenses that are classified as "other construction/design services."
-

Response

- a. None of this work was performed by a company that is an affiliate or under common ownership with Bluegrass.
- b. We evaluated engineering companies and selected a contract engineering firm that is licensed in Kentucky and has experience with water and wastewater projects of similar scale and scope. All other contractors involved in the project were subcontracted to this engineering firm and were secured by that firm.
- c. Surveying must be conducted to evaluate and map each system (especially where system maps are not available), complete the titling and easement processes involved in closing on and operating systems, properly evaluate sites for engineering design of improvements, set up billing, etc.
- d. The nature of the expenses in the "other construction/design services" include other investigative efforts executed in the planning stages of the projects conducted at each site. The exact tasks vary from site to site and include items like smoke testing, camera investigation of sewer lines, soils testing, structural evaluation, sludge depth and profiling, evaluation of regulatory compliance history and interaction, etc. All of these

are tasks required to properly plan, design, permit, and schedule construction of improvements at each site.

Request

6. Refer to Bluegrass's response to Staff DR-02-011(a). Please identify the Directors of CSWR by name.
-

Response

The Directors of CSWR are as follows:

- Josiah Cox
- John Rigas
- Daniel Standen
- Tom Rooney

Request

7. Refer to Bluegrass's response to Staff DR-02-028. Please identify the criteria by which a contractor would be "pre-qualified" to bid on project.
-

Response

Potential contractors must have experience with comparable water and/or wastewater projects, meet the minimum insurance requirements as determined by the scope of the projects being bid on, and be properly licensed in the state of Kentucky. The contractor also must express a willingness to comply with all Bluegrass's requirements and service standards, similar to those specified in Exhibit TT-2 appended to the pre-filed direct testimony of Todd Thomas.

Request

8. Refer to Bluegrass's response to AG-DR-02-008(b). Please provide any and all information upon which you rely to support your answer.
-

Response

As stated in its response to 2 AG 08, Bluegrass has not performed any studies to confirm whether the services provided by CSWR, LLC are priced no greater than market cost, but believes that the cost of services provided by non-affiliated vendors on a stand-alone basis would be more based on past experience.

Request

9. Refer to Bluegrass's response to AG-DR-02-008(a) and AG-DR-02-009. Please explain how Bluegrass allocates costs "in compliance with Bluegrass's existing cost allocation methodology," but has no cost allocation manual.
-

Response

As stated in the direct testimony of Bluegrass witness Brent Thies (pg 11, lines 1-22), the policy and methodology used by CSWR, LLC and Bluegrass Water involve allocating indirect general and administrative costs to subsidiaries using the Massachusetts allocation method. Direct costs are directly assigned to the affiliate for which the costs are incurred. The Massachusetts Formula allocates overhead costs using an average of three ratios: (1) the regulated utility affiliate's gross operating revenues to total consolidated gross operating revenues; (2) the regulated utility affiliate's gross property, plant, and equipment to total consolidated gross property, plant, and equipment; and (3) the regulated utility affiliate's gross payroll (or direct labor costs) to total consolidated gross payroll. Overhead costs are allocated to the affiliate based on the average of the three accounting items stated in the previous sentence. For purposes of this calculation, the three averages are weighted equally.

Request

10. Refer to Bluegrass’s response to AG-DR-02-009. Please identify what “financial resources” are necessary to prepare a cost allocation manual.

Response

“Financial resources” refers to costs that would be incurred to prepare a cost allocation manual (CAM), including all employee-related expense and any consulting expense that CSWR, LLC would incur to prepare the CAM. CSWR, LLC believes there is little, if any, corresponding benefits to the costs that would be incurred to create a CAM for Bluegrass Water. No other jurisdiction where a CSWR affiliate provides water or wastewater service currently requires a formal CAM. Should that requirement be imposed on Bluegrass, the expense would directly charged to that company.

Currently, all costs CSWR, LLC incurs solely for Bluegrass Water are directly charged to Bluegrass Water. Costs CSWR, LLC incurs to serve all its operating affiliates – i.e., indirect overhead costs – are allocated using the Massachusetts Method for cost allocation. As more fully described in the response to 2 INT 09, the Massachusetts Method uses three standard inputs and averages a share of each input to each operating affiliate.

Request

11. Please state whether any other affiliate operating company of Bluegrass has a cost allocation manual.

Response

No affiliate of Bluegrass Water has a cost allocation manual.

Request

12. Refer to Bluegrass’s response to Joint Intervenor-DR-01-003. Please provide the audited balance sheet, and consolidated financial statement for Bluegrass Water Holding Company, LLC for the year ending December 31, 2020. If the audited version is not yet available, consider this a continuing request.

Response

Please see the attachment labeled KY2020-00290_BW_0662 to KY2020-00290_BW_0684 for the redacted 2020 audited financials of CSWR, LLC.¹ These audited financial statements are for CSWR, LLC consolidated with all its subsidiaries, which includes Bluegrass Water Utility Operating Company, LLC (“UOC”). There is no audited balance sheet or consolidated financial statement for Bluegrass Water Utility Holding Company, LLC, because it is consolidated with UOC and is a disregarded entity for tax purposes. Please refer to the response to 1 PSC 29, including the referenced Excel file, for balance sheets as of December 31, 2020, for UOC and Kentucky CSWR, LLC.

¹ A copy of the unredacted attachment has been filed under seal with a concurrently-filed Motion seeking confidential treatment for this document.

CSWR, LLC and Subsidiaries

Consolidated Financial Statements

December 31, 2020 and 2019



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RSM US LLP

Independent Auditor's Report

Board of Directors
CSWR, LLC and Subsidiaries

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of CSWR, LLC and Subsidiaries, which comprise the consolidated balance sheets as of December 31, 2020 and 2019, the related consolidated statements of operations, member's equity and cash flows for the years then ended, and the related notes to the consolidated financial statements (collectively, the financial statements).

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the RSM audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of CSWR, LLC and Subsidiaries as of December 31, 2020 and 2019, and the results of their operations and their cash flows for the years the ended, in accordance with accounting principles generally accepted in the United States of America.

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Other Matter

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The consolidating information is presented for purposes of additional analysis rather than to present the financial position and results of operations of the individual companies and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The consolidating information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements, or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

RSM US LLP

St. Louis, Missouri
March 11, 2021

CSWR, LLC and Subsidiaries

As of December 31, 2020 and 2019

Consolidated Balance Sheets

	<u>2020</u>	<u>2019</u>
Current Assets		
Cash		
Accounts Receivable, net		
Other Current Assets		
Total Current Assets		
Property, Plant and Equipment, Net		
Non-Current Assets		
Preliminary Survey and Investigation		
Other Long-Term Assets		
Total Non-Current Assets		
Goodwill		
Intangible Assets		
Total Assets		
Current Liabilities		
Accounts Payable		
Notes Payable - Current		
Other Current Liabilities		
Total Current Liabilities		
Long-Term Liabilities		
Notes Payable, net of Current Portion		
Contributions in Aid of Construction		
Other Long-Term Liabilities		
Total Long-Term Liabilities		
Member's Equity		
Paid-In Capital		
Retained Deficit		
Total Member's Equity		
Total Liabilities and Member's Equity		

See notes to consolidated financial statements

CSWR, LLC and Subsidiaries

For the years ended December 31, 2020 and 2019

Consolidated Statements of Operations

	<u>2020</u>	<u>2019</u>
Operating Revenue		
Operating Revenue		
Operating Expense		
Operations and Maintenance		
General and Administrative		
Depreciation and Amortization		
Total Operating Expense		
Operating Loss		
Other Income (Expense)		
Other Revenue		
Interest		
Total Other Income (Expense)		
Net Loss before Taxes		
Income Tax Benefit		
Net Loss		

See notes to consolidated financial statements

CSWR, LLC and Subsidiaries

For the years ended December 31, 2020 and 2019

Consolidated Statements of Member's Equity

	Paid-In Capital	Retained Deficit	Total Member's Equity
Balance at December 31, 2018			
Capital Contributions			
Net Loss			
Balance at December 31, 2019			
Capital Contributions			
Net Loss			
Balance at December 31, 2020			

See notes to consolidated financial statements

CSWR, LLC and Subsidiaries

For the years ended December 31, 2020 and 2019

Consolidated Statements of Cash Flows

	<u>2020</u>	<u>2019</u>
Cash Flows from Operating Activities		
Net Loss		
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization		
Amortization of deferred financing costs to interest expense		
Loss on transfer of preliminary survey & investigation expense		
Loss on disposal of property, plant and equipment		
Interest capitalized to notes payable		
Interest capitalized to deferred financing costs		
Interest capitalized to allowance for funds used during construction		
Change in assets (increase) decrease		
Accounts receivable, net		
Other current assets		
Other long-term assets		
Change in liabilities - increase (decrease)		
Current liabilities		
Other long-term liabilities		
Net cash used in Operating Activities		
Cash Flows from Investing Activities		
Purchase of property, plant and equipment		
Acquisition of preliminary survey and investigation		
Net cash used in Investing Activities		
Cash Flows from Financing Activities		
Payments on notes payable		
Contributions for construction		
Capital contributions		
Net cash provided by Financing Activities		
Net Increase in Cash		
Cash, Beginning of Period		
Cash, End of Period		

See notes to consolidated financial statements

NOTE 01: NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of CSWR, LLC ("CSWR") and its wholly owned subsidiaries, Missouri Central States Water Resources, LLC ("Missouri Central States"), Arkansas Central States Water Resources, LLC ("Arkansas Central States"), Kentucky Central States Water Resources, LLC ("Kentucky Central States"), Texas Central States Water Resources, LLC ("Texas Central States") and Louisiana Central States Water Resources, LLC ("Louisiana Central States"), collectively "the Company".

The accounts of Missouri Central States' wholly owned subsidiaries are included. Those subsidiaries are: Hillcrest Utility Holding Company, Inc. ("Hillcrest"), Raccoon Creek Utility Holding Company, Inc. ("Raccoon Creek"), Indian Hills Utility Holding Company, Inc. ("Indian Hills"), Elm Hills Utility Holding Company, Inc. ("Elm Hills"), Confluence Rivers Utility Holding Company, Inc. ("Confluence Rivers") and Osage Utility Holding Company, Inc. ("Osage"), which in turn each own operating subsidiaries that carry out day-to-day operations of the Company.

The accounts of Arkansas Central States' wholly owned subsidiaries are also included. Those subsidiaries are: Hayden's Place Utility Holding Company, LLC ("Hayden's Place"), St. Joseph's Glen Utility Holding Company, LLC ("St. Joseph's Glen"), Sebastian Lake Utility Holding Company, LLC ("Sebastian Lake"), Eagle Ridge Utility Holding Company, LLC ("Eagle Ridge"), Flushing Meadows Utility Operating Company, LLC ("Flushing Meadows") and Oak Hill Utility Holding Company, LLC ("Oak Hill"), which in turn each own operating subsidiaries that carry out day-to-day operations of the Company.

The accounts of Kentucky Central States' wholly owned subsidiary, Bluegrass Water Utility Holding Company, LLC ("Bluegrass") are included. Bluegrass owns an operating subsidiary that carries out the day-to-day operations of the Company.

The accounts of Texas Central States' wholly owned subsidiary, CSWR-Texas Utility Holding Company, LLC ("CSWR-Texas") are included. CSWR-Texas owns an operating subsidiary that carries out the day-to-day operations of the Company.

The accounts of Louisiana Central States' wholly owned subsidiary, Magnolia Water Utility Holding Company, LLC ("Magnolia") are included. Magnolia owns an operating subsidiary that carries out the day-to-day operations of the Company.

The Company has additional, inactive subsidiaries which, while included in The Company's financial statements, are immaterial to the consolidated financial results.

All significant inter-company transactions and account balances have been eliminated in consolidation.

Nature of Operations and Acquisition

CSWR is a private water and wastewater utility company. The Company's primary purpose, through its subsidiaries, is to establish and maintain compliant water and wastewater treatment facilities for underserved communities and private facility owners by creating economically viable options compliant

NOTE 01: NATURE OF OPERATIONS AND BASIS OF PRESENTATION (continued)

with the Clean Water Act and the Safe Drinking Water Act. The Company holds certificates of public convenience and necessity granted by the Missouri Public Service Commission, ("Missouri PSC"), under which the Company provides water and wastewater services in Missouri. In the state of Kentucky, the Company holds certificates of public convenience and necessity granted by the Kentucky Public Service Commission, ("Kentucky PSC"), under which the Company provides water and wastewater services in Kentucky. In the state of Texas, the Company holds certificates of public convenience and necessity granted by the Public Utility Commission of Texas, ("Texas PUCT"), under which the Company provides water and wastewater services in Texas. In the state of Louisiana, the Company has been granted authority to operate water and wastewater systems by the Louisiana Public Service Commission, ("Louisiana PSC"). The Company also provides water and wastewater services in Arkansas; however, Arkansas Central States' subsidiaries are currently under the water and sewer revenue threshold that requires rate regulation from the Arkansas Public Service Commission, ("Arkansas PSC").

The Company is a wholly owned subsidiary of US Water Systems, LLC. (the "Parent").

NOTE 02: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The Company's policy is to prepare its consolidated financial statements on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America (GAAP).

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, the actual results could differ from those estimates.

Recognition of Revenue

On January 1, 2019, the Company adopted Accounting Standards Codification ("ASC") Topic 606, Revenue From Contracts With Customers using the modified retrospective approach, applied to contracts which were not completed as of January 1, 2019. Under this approach, periods prior to the adoption have not been restated and continue to be reported under the accounting standards in effect for those periods.

Under ASC 606, a performance obligation is a promise within a contract to transfer a distinct good or service, or a series of distinct goods and services, to a customer. Revenue is recognized when performance obligations are satisfied and the customer obtains control of promised goods or services. The amount of revenue recognized reflects the consideration which the Company expects to be entitled to receive in exchange for goods or services. Under the standard, a contract's transaction price is allocated to each distinct performance obligation. For contracts within the scope of ASC 606, the Company recognizes revenue through the following steps: 1) identifies the contract with a customer; 2) identifies the performance obligations within the contract; 3) determines the transaction price; 4) allocates the transaction price to the performance obligations in the contract; and 5) recognizes revenue when, or as, the Company satisfies each performance obligation.

NOTE 02: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

The Company's revenues from contracts with customers are discussed below. Customer payments for contracts are generally due within 30 days of billing and none of the contracts with customers have payment terms that exceed one year; therefore, the Company elected to apply the significant financing component practical expedient, and no amount of consideration has been allocated as a financing component.

The Company's revenue is generated from water and wastewater services delivered to customers. These contracts contain a single performance obligation, the delivery of water and wastewater services, as the promise to transfer the individual service is not separately identifiable from other promises within the contract and is not distinct. Revenue is recognized over time, as water and sewer services are provided, and includes amounts billed to customers on a cycle basis and unbilled amounts based on one month of service. The amounts the Company has a right to invoice are determined by a periodic flat fee, metered usage or both where applicable, indicating that the invoice amount corresponds directly to the value transferred to the customer. The Company elected to use the right to invoice and the disclosure of remaining performance obligations practical expedients for these revenues.

Income Taxes

CSWR, LLC has elected to be treated as a partnership for federal income tax purposes and does not record income taxes. Instead, its taxable earnings and losses are allocated in accordance with the Operating Agreement and are included in the income tax returns of the members. Accordingly, no provision is made for federal and state income taxes in the consolidated financial statements.

The Company's subsidiaries have elected to be treated as "C" Corporations. Income taxes are provided for the tax effects of transactions reported in the consolidated financial statements and consist of taxes currently due, plus deferred taxes related primarily to net operating losses timing differences.

The Company has assessed its federal and state tax positions and determined there were more likely than not no uncertainties or possible related effects that need to be recorded as of or for the years ended December 31, 2020 and 2019.

The federal and state income tax returns of the Company for the years ended December 31, 2020 and 2019 are subject to examination by the respective taxing authorities, generally for three years after they were filed.

Accounts Receivable

Accounts receivable includes utility customer accounts receivable, which represent amounts billed to water and wastewater customers on a cycle basis. Accounts receivable also includes unbilled revenue for services provided but not billed to customers. Credit is extended based on the guidelines of the applicable state regulatory body and collateral is generally not required.

The Company provides an allowance for doubtful accounts equal to the estimated losses that will be incurred in the collection of accounts receivable. This estimate is based on historical experience coupled with a review of the current status of existing receivables. The allowance and associated accounts

NOTE 02: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

receivable are reduced when the receivables are determined to be uncollectible. The allowance at December 31, 2020 and 2019 was \$100,690 and \$18,115, respectively.

Property, Plant and Equipment

Property, plant and equipment is generally stated at cost. Major additions and improvements are capitalized and, where rate regulated, placed in service subject to review and revaluation by the applicable state regulatory body, while maintenance and repairs are expensed as incurred. When assets are sold or otherwise disposed of, the related cost and accumulated depreciation are removed from the accounts. Any gain or loss arising from such disposition is included as income or expense in the year of disposition.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets. The estimated lives for computing depreciation and amortization on property, plant and equipment are:

Utility Plant in Service - Sewer	10-50 Years
Utility Plant in Service - Water	10-50 Years
Furniture, Fixtures, and Other	7-20 Years

Preliminary Survey and Investigation Charges

The Company capitalizes all expenditures for preliminary surveys, plans, investigations and other expenditures made for the purpose of determining the feasibility of the acquisition of system assets. When the acquisition of system assets occurs, these costs are reclassified to the appropriate utility plant account. If the initiative is abandoned, the costs are expensed in the period in which Management makes the determination.

Regulation

The Company's Missouri, Kentucky, Texas and Louisiana utilities are subject to economic regulation by the respective PSCs. The Missouri PSC, Kentucky PSC, Texas PUC and Louisiana PSC generally authorize revenue at levels intended to recover the estimated costs of providing service, plus a return on net investments, or rate base. The Missouri PSC approved a rate increase April 8, 2020 with an effective date of July 1, 2020 for Confluence Rivers and a rate increase December 30, 2020 with an effective date of January 29, 2021 for Elm Hills. Regulators may also impose certain penalties or grant certain incentives. Due to timing and other differences in the collection of utility revenue, an incurred cost that would otherwise be charged to expense by a non-regulated entity is (at the direction of the state PSC) to be deferred as a regulatory asset if it is probable that the cost is recoverable in future rates. Conversely, GAAP requires the recording of a regulatory liability for amounts collected in rates to recover costs expected to be incurred in the future or amounts collected in excess of costs incurred and refundable to customers.

The Company had a regulatory asset of \$50,000 ("Other Long-Term Assets"), with accumulated amortization of \$31,667 and \$21,667 at December 31, 2020 and 2019 respectively. Amortization expense for the periods ended December 31, 2020 and 2019 was \$10,000 and \$10,000, respectively.

The Company's net regulatory liability for removal costs recoverable through rates at December 31, 2020 and 2019 was \$49,583 and \$41,505 respectively. Salvage expense of the liability for removal costs was \$8,078 and \$8,069 for the periods ended December 31, 2020 and 2019 respectively.

NOTE 02: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

These liabilities are included in Property, Plant and Equipment, Net as a subset of accumulated depreciation.

Contributions in Aid of Construction

Regulated utilities may receive advances for construction and/or contributions in aid of construction from customers, home builders, real estate developers, home-owners associations, etc., to fund construction necessary to extend or enhance services or operating facilities to new areas. Advances that are no longer refundable are reclassified as contributions of capital. Contributions are permanent collections of plant assets or cash for a specific capital construction project. For tariff ratemaking purposes, the amount of such contributions generally serves as a rate base reduction since the contributions represent non-investor supplied funds. Generally, the Company depreciates utility plants funded by contributions and amortizes its contributions balance as a reduction to depreciation expense, producing a result which is functionally equivalent to reducing the original cost of the utility plant for the contributions. Amortization of contributions in aid of construction was \$1,012,555 and \$18,935 for the periods ended December 31, 2020 and December 31, 2019, respectively.

Goodwill and Other Intangible Assets

Included in the Company's financials are goodwill and intangible assets which are the result of pushdown accounting from its parent. Goodwill arising from business combinations is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized but tested for impairment at least annually or more frequently if events and circumstances exist that indicate that a goodwill impairment test should be performed. The Company has selected December 31 as the date to perform the annual impairment test. Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. Goodwill, the Trade Name and Certificate of Convenience and Necessity have an indefinite life on the consolidated balance sheets. There are no intangible assets with a definite life on the consolidated balance sheets.

New Accounting Pronouncements

In February 2016, the FASB issued Accounting Standards Update ("ASU") 2016-02, Leases: Amendments to the FASB Accounting Standards Codification, which amends the existing guidance on accounting for leases, and is effective for fiscal years beginning after December 15, 2021 for entities other than public business entities. This ASU requires the recognition of lease assets and liabilities on the consolidated balance sheets and the disclosure of key information about leasing arrangements. Early adoption is permitted and modified retrospective application is required for leases that exist or are entered into after the beginning of the earliest comparative period in the consolidated financial statements. The Company is currently evaluating the impact, if any, of adopting ASU 2016-02 on the Company's consolidated financial statements and related disclosures.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments-Credit Losses. The standard requires a financial asset (including trade receivables) measured at amortized cost basis to be presented at the net amount expected to be collected. Thus, the income statement will reflect the measurement of credit

NOTE 02: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

losses for newly recognized financial assets as well as the expected increases or decreases of expected credit losses that have taken place during the period. This standard will be effective for the calendar year ending December 31, 2022. The Company is currently in the process of evaluating the impact, if any, of adoption of this ASU on the consolidated financial statements.

NOTE 03: ASSET PURCHASES AND FACILITY OPERATIONS

Asset Purchases

Throughout the year ended December 31, 2020, the Company, through its subsidiaries, purchased certain operating assets of various previously existing companies, primarily property, plant and equipment, that provide water treatment and sewer collection and treatment services in various counties throughout Missouri, Arkansas, Kentucky, Texas and Louisiana for total cash considerations of \$38,512,048. No liabilities were assumed at acquisition. Management has determined that the cash consideration approximates the net realizable value of the assets acquired, which is indicative of the fair value. Per standard regulatory accounting procedures, \$12,057,551 of net contributions in aid of construction were recorded along with the purchased assets.

During the period ended December 31, 2019, the Company, through its subsidiaries, acquired certain operating assets of previously existing companies, primarily property, plant and equipment that provides sewer collection and treatment services, and water supply and distribution services, in various counties throughout Missouri, Arkansas, Kentucky and Louisiana for total cash considerations of \$7,159,581. No liabilities were assumed at acquisition. Management has determined that the cash consideration approximates the net realizable value of the assets acquired, which is indicative of the fair value. Per standard regulatory accounting procedures, \$564,652 of net contributions in aid of construction were recorded along with the purchased assets.

Facility Operations

During the year ended December 31, 2019, the Company, through its subsidiaries, began or continued operations at various unowned water supply and wastewater collection treatment facilities located in various counties in Missouri. In this period, the Company held or reached various agreements to acquire certain operating assets of these facilities for a total of \$572,218. The Company received regulatory approval on February 14, 2019 to complete these acquisitions and as of December 31, 2019 all acquisitions had been completed. Prior to completion of the acquisitions, the Company paid monthly operating fees totaling \$32,360 for some of these facilities.

NOTE 04: CONSOLIDATED STATEMENT OF CASH FLOWS



NOTE 04: CONSOLIDATED STATEMENT OF CASH FLOWS (continued)



NOTE 05: CASH CONCENTRATION



NOTE 06: PROPERTY, PLANT AND EQUIPMENT



Major classes of property, plant and equipment consist of the following:

	2020	2019
Utility Plant in Service - Sewer		
Utility Plant in Service - Water		
Furniture, Fixtures and Other		
Less: Accumulated Depreciation		
In Service Property, Plant and Equipment - Net		
Construction Work in Progress		
Property, Plant & Equipment Net		



NOTE 07: NOTES PAYABLE – RELATED PARTY



	2020	2019
Notes Payable balance, including accrued interest and origination fee		
Unamortized deferred financing costs		
Current portion of notes payable		
Notes Payable, net of current portion		

Future maturities of notes payable are as follows:

Years ending December 31,

2021	
2022	
2023	
2024	
2025	
Thereafter	



NOTE 07: NOTES PAYABLE -RELATED PARTY (continued)

Deferred Financing Costs



NOTE 08: OPERATING LEASE



Total future minimum commitments related to these leases are as follows:

2021 -	
2022 -	
2023 -	
2024 -	
2025 -	
Total -	



NOTE 09: EMPLOYEE BENEFIT PLAN





NOTE 10: COMMITMENTS AND CONTINGENCIES

The Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of the Company's management, the probable resolution of such contingencies will not have a material adverse effect on the financial position, cash flows or results of operations of the Company.

NOTE 11: INCOME TAXES AND LOSS CARRYFORWARD



The net deferred tax asset consists of the following components as of December 31:

	<u>2020</u>	<u>2019</u>
Accumulated net operating loss		
Allowance for doubtful accounts		
Deferred tax asset/(liability)		
Less valuation allowance		
Deferred tax asset/(liability) - Net		



NOTE 12: RECLASSIFICATIONS

Certain reclassifications have been made to the prior year consolidated financial statements to conform to the current year presentation. Total assets, total liabilities, and net loss were not affected.

NOTE 13: SUBSEQUENT EVENTS

Subsequent to year end, the Company paid approximately \$3,453,690 to acquire certain operating assets, primarily property, plant and equipment, that provides water supply and distribution services, and sewer collection and treatment services in Missouri, Texas, Kentucky and Louisiana. The assets acquired are expected to approximate the amount paid.

Management has evaluated subsequent events through the date of the independent auditors report, March 11, 2021, the date these consolidated financial statements were available to be issued.

CONSOLIDATING BALANCE SHEETS

	Consolidated	Consolidation Elimination	CSWR, LLC	Missouri-CSWR	Hillcrest	Raccoon Creek	Indian Hills	Confluence Rivers	Elm Hills	Osage	Louisiana-CSWR	Magnolia
Current Assets												
Cash												
Accounts Receivable, net												
Other Current Assets												
Total Current Assets												
Property, Plant and Equipment, Net												
Non-Current Assets												
Preliminary Survey & Investigation												
Investment in Associated Companies												
Receivable from Associated Companies												
Other Long-Term Assets												
Total Non-Current Assets												
Goodwill												
Intangible Assets												
Deferred Income Tax												
Total Assets												
Current Liabilities												
Accounts Payable												
Notes Payable - Current												
Other Current Liabilities												
Total Current Liabilities												
Long-Term Liabilities												
Notes Payable, net of Current Portion												
Payable to Associated Companies												
Contributions in Aid of Construction												
Other Long-Term Liabilities												
Total Long-Term Liabilities												
Deferred Income Tax Liability												
Members' Equity												
Paid-in Capital												
Retained Deficit												
Total Members' Equity												
Total Liabilities and Equity												

CONSOLIDATING BALANCE SHEETS

	Kentucky- CSWR	Bluegrass	Arkansas- CSWR	Hayden's Place	St. Joseph's Glen	Sebastian Lake	Eagle Ridge	Oak Hill	Flushing Meadows	TX-CSWR	CSWR-TX Operating	Inactive Entities
Current Assets												
Cash												
Accounts Receivable, net												
Other Current Assets												
Total Current Assets												
Property, Plant and Equipment, Net												
Non-Current Assets												
Preliminary Survey & Investigation												
Investment in Associated Companies												
Receivable from Associated Companies												
Other Long-Term Assets												
Total Non-Current Assets												
Goodwill												
Intangible Assets												
Deferred Income Tax												
Total Assets												
Current Liabilities												
Accounts Payable												
Notes Payable - Current												
Other Current Liabilities												
Total Current Liabilities												
Long-Term Liabilities												
Notes Payable, net of Current Portion												
Payable to Associated Companies												
Contributions In Aid of Construction												
Other Long-Term Liabilities												
Total Long-Term Liabilities												
Deferred Income Tax Liability												
Members' Equity												
Paid-in Capital												
Retained Deficit												
Total Members' Equity												
Total Liabilities and Equity												

CONSOLIDATING STATEMENT OF OPERATIONS

	Consolidated	CSWR, LLC	Missouri- CSWR	Hillcrest	Raccoon Creek	Indian Hills	Confluence Rivers	Elm Hills	Osage	Louisiana- CSWR	Magnolia
Operating Revenue											
Operating Revenue											
Operating Expense											
Operations and Maintenance											
General and Administrative											
Depreciation and Amortization											
Total Operating Expense											
Operating Loss											
Other Income (Expense)											
Other Revenue											
Interest											
Total Other Income (Expense)											
Net Loss before Taxes											
Net Income (Loss)											

CONSOLIDATING STATEMENT OF OPERATIONS

	Kentucky- CSWR	Bluegrass	Arkansas- CSWR	Hayden's Place	St. Joseph's Glen	Sebastian Lake	Eagle Ridge	Oak Hill	Flushing Meadows	TX-CSWR	CSWR-TX Operating	Inactive Entities
Operating Revenue												
Operating Revenue												
Operating Expense												
Operations and Maintenance												
General and Administrative												
Depreciation and Amortization												
Total Operating Expense												
Operating Loss												
Other Income (Expense)												
Other Revenue												
Interest												
Total Other Income (Expense)												
Net Loss before Taxes												
Net Income (Loss)												

Request

13. Refer to Bluegrass's response to Joint Intervenor-DR-01-005. Please identify any actual or potential conditions any prospective lender has, or is anticipated to, impose with regard to the outcome of this rate case.
-

Response

The term sheet/offer related to proposed permanent financing for Bluegrass Water contains no condition expressly related to the outcome of this rate case. However, because *pro forma* financial data provided to the potential lender included projections related to Bluegrass Water's current and future rate cases, and because any loan would be contingent on a representation that Bluegrass Water has experienced no material adverse change to its financial condition, a negative rate case outcome could adversely affect the company's ability to secure debt financing and/or the interest rate for such financing.

Request

14. Please state whether Bluegrass's capitalization should be imputed for ratemaking purposes to something less than its current actual capitalization of 100% equity?

Response

Bluegrass Water has proposed a hypothetical capital structure of 50% equity and 50% debt for ratemaking purposes.

Request

15. Please identify whether Midwest Water Operations, LLC, served any water or wastewater systems in Kentucky prior to entering into agreements for systems owned by Bluegrass.

Response

To Bluegrass Water's knowledge, Midwest Water Operations, LLC, did not serve any water or wastewater systems in Kentucky prior to entering into agreements for Bluegrass systems.