

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION OF KENTUCKY

In the Matter of:

Electronic Application of Water Service)	
Corporation of Kentucky for a General)	
Adjustment in Existing Rates and a Certificate)	Case No. 2022-00147
of Public Convenience and Necessity to Deploy)	
Advanced Metering Infrastructure and Approval)	
of Certain Regulatory Accounting Treatment)	

**RESPONSE BRIEF OF
WATER SERVICE CORPORATION OF KENTUCKY**

Water Service Corporation of Kentucky (“WSCK” or the “Company”) seeks an increase in rates for water service and a certificate of public convenience and necessity to deploy advanced metering infrastructure. On December 16, 2022, the Office of the Attorney General (“OAG”) and City of Clinton (“City”) (collectively, “OAG/City”) filed a joint Initial Brief. WSCK, by counsel, respectfully submits this Response Brief addressing some of the arguments presented in the OAG/City’s Initial Brief. In the interests of administrative economy, WSCK also fully adopts and incorporates its arguments presented in its Initial Brief, which addresses nearly all of the OAG/City’s arguments. Silence on any particular issue should not be construed as acceptance by WSCK of opposing arguments.

I. Monthly Customer Charge

Despite providing no testimony to support its argument, the OAG/City attempt to argue that an increase in the monthly customer charge is unreasonable because it poses a financial hardship on some residential customers. They propose that any increase in rates be only applied

to the volumetric rate. Alternatively, they propose that the increase to the monthly charge be phased in over two years.¹ There are several flaws with the OAG/City's argument.

First, as mentioned above, the OAG/City have not presented any testimony on this issue. The Commission has explained that when intervening parties submit data requests to parties but offer no evidence or testimony on those issues, the Commission has no evidentiary basis to support the intervening parties' proposed adjustments to the utility's case.² Under these circumstances, the Commission has approved the utility's proposals.³ Accordingly, the Commission does not have any basis to accept the OAG/City's proposed adjustment to the monthly customer charge.

Second, the Commission has specifically found that an across-the-board uniform increase is appropriate when there has not been a cost-of-service study prepared and when there has been no evidence demonstrating that uniform increase is unreasonable.⁴ As such, the Commission should reject the OAG/City's request.

Third, WSKC operates in a mostly fixed-cost business. As such, the utility should be allowed to use a rate structure that reflects the fixed cost environment in which it operates. This requires an increase to the monthly customer charge consistent with the increases in cost of service.

Fourth, the OAG/City's alternate proposed phased-in approach does not produce benefits as substantial as the OAG/City suggest. By reducing the monthly customer charge collected by

¹ OAG/City Initial Brief at 4-5.

² See [Kentucky-American Water Co.](#), Case No. 2018-00358 (Ky. PSC June 27, 2019) (“The Commission notes that the Attorney General and LFUCG submitted data requests to Kentucky-American regarding the chemical complex but offered no evidence or testimony regarding the ratemaking treatment of the chemical complex. The Commission’s findings must be supported by sufficient evidence. Here, with no evidentiary support in the record regarding the proposed adjustment, the Commission is without any basis, much less sufficient evidence, to justify an adjustment, and therefore we deny LFUCG’s proposed adjustment to remove expenses related to constructing the chemical complex.”)

³ *Id.*

⁴ [Southeast Daviess County Water District](#), Case No. 2020-00195 at 11 (“The Commission finds that the allocation of a revenue increase evenly across the board to a utility’s rate design is appropriate when there has been no evidence entered into the record demonstrating that this method is unreasonable and in the absence of a COSS.”)

the utility, the volumetric charge must increase in order to ensure that the utility has the opportunity to recover its revenue requirements.⁵ Moreover, the alternate phased-in approach could create consumer confusion. Initially, the volumetric rate would have a disproportionate increase, but then decrease when Phase 2 is implemented in order to reflect the same authorized revenue requirement. This would create conflicting price signals to customers. Also left unaddressed in the OAG/City's proposal is consideration for any adjustment to the volumetric tiers in the Company's rate structure.

For the foregoing reasons, the Commission should reject the OAG/City's proposals on this issue.

II. Certificate of Public Convenience and Necessity for Advanced Metering Infrastructure

The OAG/City recommend the Commission deny WSCK's requested certificate of public convenience and necessity ("CPCN"), but their arguments are hollow. The OAG/City maintain that WSCK did not demonstrate an inadequacy of existing service. This, however, is a short-sighted position. If the Commission were to accept the OAG/City's argument, utilities would be required to allow facilities to fail prior to issues being addressed. Obviously, the prudent practice requires timely and proactive replacement of infrastructure prior to failure in order to maintain or improve service. And that is precisely what WSCK proposes to do.

Along these lines, the OAG/City assert that the CPCN should be denied because the current meters are providing reliable service. The OAG/City seemingly ignore, however, several critical facts in evidence. First, the meters in the City of Clinton are at the end of their useful life and the

⁵ The cases cited by the Attorney General acknowledge that the volumetric rate must increase when the fixed rate decreases. See [Kentucky Power Co.](#), Case No. 2014-00396 (Ky. PSC June 22, 2014); [Louisville Gas & Elec. Co.](#), Case No. 2000-00080 (Ky. PSC Sept. 27, 2000).

AMR technology will no longer be maintained by the manufacturer.⁶ Second, WSCK is experiencing an upward trend of meters requiring re-reads.⁷ This duplicative work generates staffing burdens for WSCK, which ultimately WSCK customers will bear if the current metering system is not upgraded. Third, customers will see significant benefits from AMI with the ability to monitor water consumption and cost information to better manage their personal water usage.⁸ These reasons demonstrate the need for the AMI system.

With respect to the Commission’s “wasteful duplication” standard, the OAG/City provided no support for their conclusory statement that WSCK’s system “should not be considered a consumer market large enough to make the AMI project economically feasible.”⁹ In contrast, WSCK has demonstrated economic feasibility based on the evidence that the revenue requirement will be decreased based on a negative revenue requirement impact for the Forecast Period related to this AMI project.¹⁰ The conclusion advocated by the OAG/City would also preclude a slew of system modernization efforts that the Company may undertake, including AMI or SCADA, simply due to its relatively small customer base.

The OAG/City also argue that WSCK did not consider reasonable alternatives because it did not have Vaughn & Melton prepare a cost-benefit analysis until after the underlying Application was filed.¹¹ But contrary to the OAG/City’s argument, the evidence demonstrated that WSCK and its corporate parent did evaluate several options through a process that involved multiple vendors bidding on AMI implementation.¹² Moreover, the Vaughn & Melton report was prepared by an engineering firm who had no prior engagement with WSCK, which demonstrates

⁶ Response to [PSC 3-18](#).

⁷ Response to [PSC 2-19\(d\)](#).

⁸ [Wilson Direct](#) at 10.

⁹ OAG/City Initial Brief at 9.

¹⁰ See WSCK’s Initial Brief at 13 n. 70.

¹¹ OAG/City Initial Brief at 10.

¹² Response to PSC 2-19 (filed confidentially).

neutrality of the author. The report was submitted in this matter to further demonstrate the reasonableness of WSCK's proposal and the benefits of an AMI rollout.

The OAG/City criticize WSCK for not including “*potential* ongoing savings attributable to the proposed AMI project in the proposed revenue requirement in the pending case.”¹³ The OAG/City fail to acknowledge that there is an inherent limitation to recognizing savings in this proceeding due to the phase-in approach of the Company's AMI implementation and the forward-looking basis for setting rates, which requires reasonable support for the forecasted costs of service. Due to the multi-year rollout of the AMI system, any realized savings would effectively have minimal impact in the Forecast Period. If there are realized savings, they will be maximally accrued over the entire deployment and addressed in future rate cases.

The OAG/City also maintain that the AMI project should be denied because there will be depreciation expense remaining on the books related to some of the meters that are removed. The remaining depreciation expense, however, is a by-product of the 44.4-year depreciation life of a meter. The Commission has approved CPCNs for multiple water utilities seeking installation of AMR/AMI systems despite the fact that some of their meters were less than ten years old and, thus, carrying “stranded costs” after the change.¹⁴ Accordingly, this is not prohibitive to AMI deployment.

WSCK submits that it has appropriately demonstrated a need for the AMI system and that it will not result in wasteful duplication. Accordingly, approval of the CPCN is appropriate.

¹³ OAG/City Initial Brief at 9 (emphasis added).

¹⁴ See [Henderson County Water Dist.](#), Case No. 2014-00402 at 2 (Ky. PSC Feb. 3, 2015)(stating that the utility would initially focus on areas of the system where most meters are older than ten years old “and then proceed to replace newer meters”); [Southeast Daviess County Water District](#), Case No. 2020-00195 at 2 (inferring that there are meters in the system less than 10 years old).

III. Rate Base Issues

A. JDE and Oracle Enhancements

The OAG/City maintain that WSKC's rate base should not include enhancement costs for J.D. Edwards financial software system and the Oracle Customer Care and Billing system enhancement costs.¹⁵ Notably, the OAG/City have never argued that these enhancements do not benefit customers. In addition, these enhancements are required and implemented to maintain assets, and provide customer benefits such as improved options for managing customer billing and collections, as well as operational efficiencies, such as improved reporting and cost tracking and management functionality.¹⁶ These enhancements were NOT part of Project Phoenix, as they occurred several years later and are separate and distinct from the considerations of the WSKC's 2008, 2010, and 2013 rate cases.

B. Deferred Rate Case Expense Inclusion in Rate Base

In its Initial Brief, WSKC fully and adequately addresses the OAG/City's arguments related to WSKC's inclusion of deferred rate case expense in rate base.

C. ADIT and Bad Debt Expense

Without citing any precedent from Kentucky or elsewhere, the OAG/City maintain that WSKC's requested revenue requirement should not include the recovery of Accumulated Deferred Income Tax ("ADIT") balances for two assets: Deferred Federal Tax-Bad Debt and Deferred State Tax-Bad Debt. Notably, the AG/City's argument is inconsistent with their proposal regarding Cash Working Capital—i.e., the fact that uncollectibles are expected to occur represents collection lag and therefore a need for Cash Working Capital.

¹⁵ OAG/City Initial Brief at 3-4.

¹⁶ [DeStefano Rebuttal](#) at 4.

D. Cash Working Capital

Consistent with prior WSCK rate cases,¹⁷ WSCK included a cash working capital allowance in its requested recovery in rate base, based on the 1/8th operations and maintenance expense methodology. In those prior cases, the Commission recognized the limited cost/benefit to such a small utility performing a potentially costly study when a simpler, previously approved method is available. The Company's link to a larger parent company is irrelevant to the implications to the Company's customers of performing a study and recovering its costs; a lead/lag study would need to be performed for and reflective of WSCK, not its parent company.¹⁸ Moreover, industry guidance further demonstrates the reasonableness of WSCK's approach. The AWWA M-1 manual states that "Determining working capital requires estimates (sometimes in total or in great detail) of the lag between paying expenses and receiving revenue. This determination is sometimes simplified by using one-eighth (45 days) of O&M expenses as a reasonable surrogate for a more formal lead-lag study."¹⁹ Accordingly, WSCK requests continued treatment of the previously approved methodology for calculating Cash Working Capital.

IV. Rate of Return Issues – Return on Equity

The comprehensive Direct and Rebuttal Testimonies Dylan D'Ascendis adequately address the arguments of the OAG/City's Initial Brief, as it relates to return on equity ("ROE").

There are two points worth emphasizing.

¹⁷ See, e.g., [Water Service Corp. of Kentucky](#), Case No. 2020-00160 at 4 (Ky. PSC Dec. 8, 2020)(holding that 1/8th method is a "reasonable approach for Water Service Kentucky, particularly given its size and relative sophistication, and the Commission will permit its use in this matter given those factors.").

¹⁸ If Cash Working Capital was tied to a utility's parent company, sister subsidiaries could negatively impact another operating utility that has better individual metrics.

¹⁹ American Water Works Association, *Manual of Water Practices, Principals of Water Rates, Fees, and Charges* at 44 (6th ed. 2012)

First, the OAG/City inaccurately suggest that the Commission has never authorized a size adjustment to ROE.²⁰ In WSCK's last rate case in which revenue requirement was based on rate base/rate of return, WSCK proposed a 35-basis point addition to its proposed ROE based on its small size.²¹ The Commission approved this adjustment, stating: "The approved 10.6 percent ROE includes a size adder as proposed by the company."²²

Second, the OAG/City argue that WSCK is "a low-risk water utility," but there is no evidence in the record supporting such a determination.²³ WSCK has experienced low returns historically, has not been approved for recovery mechanisms, and is extremely small in size. All of this is true despite the support of WSC and a larger corporate parent. As D'Ascendis testified, investors are interested in the returns of an operating utility, such as WSCK, because those returns are what drive the jurisdictional results and that entity is ultimately where investment is made.²⁴ The analysis, thus, should not go up the ladder to consideration of a larger parent when assessing risk relevant to WSCK.

For these reasons and the reasons stated in D'Ascendis's testimonies, WSCK respectfully requests a 10.6% ROE.

V. Expense Issues

A. Payroll Expenses and Payroll Taxes

In its Initial Brief, WSCK fully and adequately addresses the OAG/City's arguments related to WSCK's payroll expense and taxes to be included in revenue requirements. WSCK nevertheless notes that the OAG/City's arguments related to health insurance premiums are

²⁰ OAG/City Initial Brief at 29-30.

²¹ [Water Serv. Corp. of Kentucky](#), Case No. 2008-00563 at 23.

²² *Id.* at 24.

²³ OAG/City Initial Brief at 28.

²⁴ [D'Ascendis Direct Testimony](#) at 44-46.

intertwined with WSCK's payroll expenses and taxes. If the Commission were to accept the OAG/City's position on health insurance premiums and reduce the amount of expense recovered in revenue requirement, it would be inappropriate to further exclude payroll expense on the basis of the OAG/City's argument that WSCK's 2022 payroll expenses, including benefits, was slightly above the market midpoint. Exclusion of both amounts would be duplicative.

B. Incentive Compensation

In its Initial Brief, WSCK fully and adequately addresses the OAG/City's arguments related to allocated incentive compensation to be included in revenue requirements.

C. Health Insurance Expense and Premiums

In its Initial Brief, WSCK fully and adequately addresses the OAG/City's arguments related to health insurance expense and premiums to be included in revenue requirements.

D. Legal Expenses

In its Initial Brief, WSCK fully and adequately addresses the OAG/City's arguments related to legal expenses to be included in revenue requirements.

E. Rate Case Expense

The arguments in WSCK's Initial Brief demonstrate that WSCK has incurred reasonable rate case expense associated with this matter. The OAG/City myopically maintain that WSCK's utilization of two law firms makes the legal expense associated with the rate case unreasonable. The number of law firms, or even attorneys, dedicated to a particular case is not indicative of the reasonableness of expenses related to the service they provide. Rather, the total expense in comparison to the scope of necessary work is a much stronger factor on which to evaluate reasonableness.

WSCK's total rate case expense is undoubtedly reasonable, as the comparison between this case and Kentucky-American Water Company's last rate case demonstrates. Even with the removal of three categories of expenses in the Kentucky-American case that were not applicable to WSCK's case, WSCK's rate case expense is approximately one third the amount of Kentucky-American's (\$311,992 in comparison to \$918,735).²⁵ Similarly, WSCK incurred far less in legal expense (\$164,654 versus \$521,550 and 475 hours versus 1,150 hours).²⁶ This comparison cannot be discounted simply because Kentucky-American is a larger utility. Both cases had the same minimum filing requirements, multiple expert reports and testimony, and hundreds of data requests propounded upon the utility. Thus, should Kentucky-American's expense be acceptable (as the Commission found), WSCK's far smaller expense should likewise be acceptable.

The OAG/City's discussion of the requested revenue increase is not relevant to this issue. There is a baseline level of support a utility must provide when a rate case is filed and processed, as detailed above. Also, WSCK is entitled the opportunity to earn a reasonable rate of return on its investment.²⁷ Even the OAG/City's expert witnesses acknowledge that WSCK should be authorized an increase to its revenue requirement of at least \$456,911.²⁸ The only mechanism by which WSCK would have an opportunity to earn that additional revenue is through the current proceeding. And the legal services provided by Sturgill Turner and Ice Miller were necessary to prepare and litigate this case. Accordingly, it would be confiscatory not to allow WSCK to recover its rate case expense in rates.

²⁵ See WSCK Initial Brief at 33-34.

²⁶ *Id.* at 35.

²⁷ See *Fed. Power Co. v. Hope Natural Gas Co.*, 320 US. 591 (1944); *Bluefield Water Works v. Pub. Serv. Comm'n of West Virginia*, 262 US. 679 (1923).

²⁸ See Furtal Direct Testimony at 5.

The OAG/City’s suggestion that additional “scrutiny” be placed on WSCK’s and its parent’s in-house legal expense mischaracterizes the testimony in this case. In saying that WSCK “does not have access to internal legal counsel,” the OAG/City completely ignore the entirety of the testimony that stated WSCK “does not have an internal legal counsel dedicated to regulatory support.”²⁹ There is a stark contrast between the picture the OAG/City unfairly attempts to paint on this issue and reality. Moreover, the intervenors had the opportunity to scrutinize the evidence, including testimony, of WSCK’s Corporate Services expenses in this case, and they did not identify any criticism in their testimony.

Finally, the OAG/City erroneously argue that a utility’s utilization of multiple law firms in a rate case is “nearly unprecedented.” However, for example, municipalities commonly utilize multiple law firms for rate case litigation, particularly when one has primary knowledge of the municipal utility and another has greater knowledge on regulatory procedure before the Commission.³⁰ Multiple law firms have also been utilized by utilities generally under Commission jurisdiction in rate cases.³¹

For these reasons, WSCK requests that the Commission reject the OAG/City’s arguments on this issue and find that WSCK’s rate case expense is reasonable.

F. Bad Debt Expense

In their Initial Brief, the OAG/City add an alternative argument to suggest that the Commission could approve bad debt expense based on 2.73%, which is derived from October 2021 to September 2022. But the OAG/City undercut their own alternative argument by asserting that

²⁹ [Kilbane Rebuttal](#) at 8 (emphasis added).

³⁰ See, e.g., [City of Pikeville](#), Case No. 2019-00080, VR: 9/11/19, in which both the municipal utility and intervenor were each represented by attorneys with two separate firms; [City of Augusta](#), Case No. 2015-00039 (Ky. PSC Apr. 15, 2016).

³¹ See, e.g., [Big Rivers Elec. Coop.](#), Case No. 2013-00199 (Big Rivers’ Post-Hearing Brief, filed Feb. 14, 2014).

2020 and 2021 were “strong outliers due to the pandemic.” In contrast, WSCK has demonstrated that it is still seeing near pandemic-level uncollectibles accruing since it resumed normal collections in October 2021.³²

In contrast to the OAG/City’s inconsistent assertions, WSCK’s recommended 3.93% for bad debt is reasonable. It is based on an appropriate mix of pre-pandemic and pandemic periods that are more representative of the current and ongoing collections activities. It is further verified by the last nine months that has reflected a 3.7% uncollectible rate. Accordingly, WSCK requests that the Commission reject the OAG/City’s argument on this issue.

VI. Conclusion

WSCK has met its burden of proof in this case with the appropriate modifications noted in its Initial Brief. Accordingly, WSCK requests the Commission approve an increase in rates and the CPCN for an AMI program.

Respectfully submitted,



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³² See [Kilbane Rebuttal](#) at 7.