COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF KENTUCKY-AMERICAN WATER COMPANY FOR AN ADJUSTMENT OF WATER RATES, APPROVAL OF SYSTEM IMPROVEMENT PROGRAM, AND TARIFF CHANGES	))))	CASE NO. 2026-00094

THE ATTORNEY GENERAL, LEXINGTON-FAYETTE URBAN COUNTY GOVERNMENT, AND GEORGETOWN MUNICIPAL WATER AND SEWER SERVICE'S RESPONSE TO THE COMMISSION STAFF'S FIRST REQUEST FOR INFORMATION

The intervenors, the Attorney General of the Commonwealth of Kentucky, through his Office of Rate Intervention ("Attorney General"), Lexington-Fayette Urban County Government ("LFUCG"), by counsel, and Georgetown Municipal Water and Sewer Service ("GMWSS"), by counsel, submit the following response to the Commission Staff's First Request for Information in the above-styled matter.

Respectfully submitted,

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<u>Certificate of Service and Filing</u>

Pursuant to the Commission's Orders and in accord with all other applicable law, Counsel certifies that the foregoing electronic filing was transmitted to the Commission on September 10, 2026, and there are currently no parties that the Commission has excused from participation by electronic means in this proceeding.

This 10th day of September, 2026,

Angela M. Awad

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Assistant Attorney General

WITNESS RESPONSIBLE:
JOHN DEFEVER

QUESTION NO. 1
Page 1 of 1

Refer to the Direct Testimony of John Defever (Defever Direct Testimony), page 40. Explain in detail what customer protections would be appropriate for the proposed System Improvement Program (SIP) mechanism.

RESPONSE:

As discussed in my testimony, customer protections could include, but not be limited to, the following prior restrictions that the Commission had placed on Kentucky-American Water Company's ("Kentucky American") prior pipeline replacement program:

- Limitations on the miles of pipeline that could be replaced annually;
- The type of pipeline that could be replaced; and,
- Restrict to projects that are related to replacing aging mains.

Additionally, further limitations that would provide customer protection could include a specific annual cost limitation allowed to flow through the proposed SIP.

WITNESS RESPONSIBLE:
JOHN DEFEVER

QUESTION NO. 2
Page 1 of 2

Refer to the Defever Direct Testimony, pages 26-27.

a. State whether the Kentucky Public Service Commission has approved a similar adjustment to reduce recoverable Board of Directors Expense. If so, identify each case and provide the relevant order.

b. Provide the rationale for the 75/25 percent split between shareholders and ratepayers.

c. Confirm that other public utility commissions or relevant retail regulatory authorities outside of the Connecticut Public Utilities Regulatory Authority (PURA), have made a similar adjustment to reduce a utility's board of directors expenditures. If confirmed, provide the other regulatory authority's decision on the matter and provide a narrative description of the adjustment made in each docket.

RESPONSE:

a. I am not aware that the Kentucky Public Service Commission has approved a similar adjustment; however, it is my understanding that the Commission is not bound by its prior rulings on a specific issue.

b. The rationale behind the 75/25 split of the Board of Directors' Expense is due to shareholders receiving the majority of the benefits while ratepayers receive less of the benefits; thus, a sharing of less than 50/50 for ratepayers is appropriate.

c. While I have not conducted an exhaustive search, I am aware that the Arizona Corporation Commission has disallowed all or portions of Board of Directors' expenses. The following cases are examples:

   Decision No. 80326 (April 7, 2025) in Docket No. G-01551A-23-0341, stated the following on page 48:

   > "As Decision Nos. 79065 and 79293 explained in the language repeated here, the Commission is of the view that the Board of Directors serves primarily to support the interests of the shareholders. As RUCO notes, the applicant bears the burden of proof that an expense would be just and reasonable for recovery from ratepayers. We find no evidence in the record that persuasively argues for ratepayers to bear

> these costs. Consequently, we find that RUCO's recommendation to disallow the cost of Board of Directors is reasonable and should be adopted."[1]

In Decision No. 79065 (August 25, 2023), in Docket No. E-01933A-22-0107, the Arizona Corporation Commission stated the following at pages 38-39:

> "We note that Board of Directors are elected by the shareholders to serve the shareholders. The Board of Directors has such responsibilities as choosing the corporate officers, distributing dividends, authorizing stock issuance, determining whether to merge with another corporation, and setting strategy. As such, all expenses associated with the Board of Directors should be borne by shareholders. We will disallow the Board of Directors fees of $712,273 in this case; therefore, these fees shall not be borne by ratepayers."[2]

[1] *See* https://docket.images.azcc.gov/0000213430.pdf?i=1789002813700.
[2] *See* https://docket.images.azcc.gov/0000209684.pdf?i=1789045587898.

WITNESS RESPONSIBLE:
AARON L. ROTHSCHILD

QUESTION NO. 3
Page 1 of 1

Refer to the Direct Testimony of Aaron L. Rothschild (Rothschild Direct Testimony), generally.

a. Provide Exhibits ALR-1 through ALR-10 in Excel spreadsheet format with all columns, rows, and formulas unprotected and fully accessible.

b. For all sources which reference the "most current data available at time of schedule preparation," provide the date the data was prepared or accessed.

RESPONSE:

a. Please see Exhibits ALR-1 through ALR-10 in Excel Spreadsheet format being filed contemporaneously with the discovery responses that are in "2026.06.30 - KAWC Cost of Capital (RFC Water PG).xlsx" and "2026.06.30 - KAWC Cost of Capital (Bulkley PG).xlsx."

b. May 22, 2026, for financial data from gas utility data and April 3, 2026, for water utility data.

WITNESS RESPONSIBLE:
AARON L. ROTHSCHILD

QUESTION NO. 4
Page 1 of 1

Refer to the Rothschild Direct Testimony, page 10, lines 8-12. Explain why using the absolute median of the return-on-equity (ROE) results would constitute a reasonable strict mathematical approach. Identify the factors that would support selecting a different percentile within the range.

RESPONSE:

The median is my estimate of Kentucky American's market-based cost of equity. As explained at pages 10–11 in my direct testimony, I do not recommend that the Commission adopt the median immediately. The factor that supports selecting a percentile above the median is the regulatory principle of gradualism. Authorized returns across the industry have not yet adjusted to the decline in market-based costs of equity. Moving in a single proceeding from prevailing authorized levels to the market median would be an abrupt change. The principle of gradualism, which the Commission has applied in the context of rate adjustments, supports a measured transition toward the market-based cost of equity rather than an immediate one. This is the reason my recommendation lies in the upper portion of my results.

This factor supports a return above the median. It does not support a return above the range of my results, and it does not support treating authorized returns in other jurisdictions as evidence of the cost of equity, for the reasons given at pages 85–87 of my direct testimony. Authorized returns are accounting returns on book value; investors purchase equity at market value, and the price they pay already reflects their expectations regarding regulatory treatment. Other jurisdictions' authorized returns are therefore relevant to the pace at which authorized returns should converge toward market costs, not to what those costs are. My recommendation of 8.07%, the 85th percentile of my results, reflects my judgment as to how far above the market median gradualism warrants moving.

WITNESS RESPONSIBLE:
AARON L. ROTHSCHILD

QUESTION NO. 5
Page 1 of 1

Refer to the Rothschild Direct Testimony, page 11, lines 10-11. Further explain how the distribution of results supports a range between the 80th and 90th percentiles, rather than a different range, specifically as it relates to this proceeding.

RESPONSE:

The percentile range I apply is not selected in the abstract. The regulatory principle of gradualism, discussed at pages 10–11 of my direct testimony, establishes the objective: a recommendation that moves toward the market-based cost of equity, which my results place at a median of 6.93%, without an abrupt departure from prevailing authorized returns, and that remains within the results my models produce. The distribution of results determines where that objective falls in percentile terms.

In this proceeding, the fourteen results in Table 2 and Exhibit ALR-2 fall into two groups. The eight CAPM results and the two option-implied-growth DCF results cluster between 5.32% and 7.30%. The non-constant-growth DCF results (7.91% and 7.99%) and the sustainable-growth DCF results (9.59% and 9.66%) lie above them. The 80th percentile, 7.95%, is the point at which the distribution moves from the first group into the second; beginning the range there gives effect to the upper portion of the distribution, consistent with gradualism. The 90th percentile, 9.11%, is where the range ends because above that point the distribution consists of the sustainable-growth DCF results alone, and a recommendation above the 90th percentile would rest on a single method rather than on the distribution of results.

WITNESS RESPONSIBLE:
AARON L. ROTHSCHILD

QUESTION NO. 6
Page 1 of 1

Refer to the Rothschild Direct Testimony, page 11, lines 15-16. Explain the reasonableness of giving the same weight to all ROE analyses performed. In the response, explain whether any of the analyses are more reasonable than others and if so, why.

RESPONSE:

The referenced passage states that my results, "do not depend on selecting any one model or result over another." This is not a weighting scheme. I do not compute a weighted average. I present every result produced by the models I apply, no results are removed at any stage, and I apply a percentile range to the complete set, so each result enters the distribution once.

I treat the results this way for two reasons. First, each model in my analysis is already the version of that model I consider most reliable, for the reasons explained in my testimony (for example, at page 25 and Appendix D). Those judgments are made at the model-design stage; they are not applied a second time by discarding or discounting results after the fact. Second, the DCF and CAPM rely on different inputs and assumptions, and the variations within each capture different information. A recommendation drawn from the full distribution is less sensitive to the estimation error of any single model, and applying a transparent percentile range avoids the subjective and readily disputed judgment that explicit weighting would require.

As to whether any of the analyses are more reasonable than others: the comparisons drawn in my testimony are between the methods I apply and alternatives I do not apply. Among the methods I do apply, each has recognized strengths and limitations, and I do not consider any of them so much more reliable than the others that its results should displace theirs.

WITNESS RESPONSIBLE:
AARON L. ROTHSCHILD

QUESTION NO. 7
Page 1 of 1

Refer to the Rothschild Direct Testimony, page 23, lines 2-4. Specify which proxy group companies have unregulated gas operations and any other unregulated operations and explain why the increased risk is not cause to exclude the company from the proxy group.

RESPONSE:

The companies in the proxy group with non-regulated operations are American States Water (contracted water and wastewater services at U.S. military installations, 18.0 percent of 2025 net income), Chesapeake Utilities (propane distribution, unregulated natural gas gathering, etc, 13.1 percent of 2025 operating income), and NW Natural Holdings (a small non-regulated renewable natural gas business reported outside its regulated segments). Spire completed the sale of its gas marketing business on April 30, 2026, and Southwest Gas completed its exit from Centuri on September 5, 2025; both now consist of regulated operations. The remaining companies have no material unregulated operations.

These operations are not cause for exclusion because the proxy group is the one selected by the Company's own witness, Ms. Bulkley, as comparable in risk to Kentucky American; I adopted it so that differences in results would reflect differences in method rather than sample.

WITNESS RESPONSIBLE:
AARON L. ROTHSCHILD

QUESTION NO. 8
Page 1 of 1

Refer to the Rothschild Direct Testimony, page 27, lines 8-10.

a. Explain whether all methods of obtaining the stock price were considered equally, or if more weight was given to the average stock price or spot value.

b. Compare and contrast this methodology versus only using an average stock price such as the six-month average stock price or three-month average stock price.

RESPONSE:

a. Both methods were considered equally. As shown in Exhibit ALR-3, page 1, I calculated the DCF cost of equity twice: once using the closing stock price on June 30, 2026 and once using the average of the high and low stock prices for the twelve months ending June 30, 2026. Each calculation produces its own result, and each result enters my overall distribution once, on the same terms as every other result. No additional weight is given to either the spot price or the average price. This is consistent with my general approach, described at pages 19–22 of my direct testimony, of using both recent spot data and historical averages for market inputs wherever possible.

b. Using only an average stock price, whether over three, six, or twelve months, treats the price as though it were stationary over that period and discards the information contained in where the price currently is relative to that average. As illustrated at page 20 of my direct testimony, two stocks can have identical average prices over a period while one has risen and the other has fallen, and a forward-looking analysis that used only the average would treat them identically even though the most recent data points toward different near-term prices. Conversely, using only a spot price exposes the result to the fluctuations of a single day. Using both, as I do, captures the stability of the average and the recency of the spot value, and presenting both results rather than blending them allows the Commission to see the effect of the choice directly. A single three- or six-month average would provide neither the recency of a spot value nor the smoothing of a full-year average.

WITNESS RESPONSIBLE:
AARON L. ROTHSCHILD

QUESTION NO. 9
Page 1 of 1

Refer to the Rothschild Direct Testimony, page 35, lines 9-11. Provide why it is appropriate to use weighted averages over three months, rather than a longer time horizon as seen in some of the other analyses.

RESPONSE:

As explained at pages 19–21 of my direct testimony, market inputs such as stock prices, betas, and risk premia fluctuate, and a forward-looking analysis should reflect both the stability of historical averages and the information in the most recent data. My Spot CAPM uses values as of June 30, 2026. My Weighted Average CAPM uses the three months ending on that date, with more weight given to the more recent weeks, as shown in Exhibit ALR-4, page 3. A three-month, recency-weighted average is long enough to smooth day-to-day fluctuations but short enough that the result reflects current market conditions rather than conditions that have since changed. It also corresponds to the period over which the option-implied inputs are measured (pages 44–45). A three-month, or 90-day, averaging period is also commonly used by cost of capital analysts in rate proceedings; Ms. Bulkley, for example, includes a 90-day average among the averaging periods in her DCF analysis.

WITNESS RESPONSIBLE:
AARON L. ROTHSCHILD

QUESTION NO. 10
Page 1 of 2

Refer to the Rothschild Direct Testimony, page 6, Table 1, which reflects recommended cost rates of 8.50 percent for preferred equity and 8.07 percent for common equity. Refer also to the Application, Direct Testimony of Ann E. Bulkley (Bulkley Direct Testimony), page 5, lines 1-9, and page 50, lines 1-5, where Ms. Bulkley recommends a 10.75 percent ROE within a range of 10.25 percent to 11.25 percent.

a. Explain how a common-equity cost rate below the preferred-equity cost rate is consistent with the relative risk and priority of claims associated with common and preferred equity.

b. State whether a rational investor would generally require a higher expected return for common equity than for preferred equity and explain the response.

c. Explain why an 8.07 percent ROE remains reasonable when it is lower than the 8.50 percent preferred-equity cost rate reflected in the same table, and state whether the recommended common-equity ROE should be adjusted to no less than the preferred-equity cost rate.

d. State whether Mr. Rothschild considers any ROE between his 8.07 percent recommendation and Ms. Bulkley's 10.75 percent recommendation reasonable for Kentucky-American. If so, identify the portion of that interval he considers reasonable and explain the factors the Commission should weigh in selecting a point within it. In the response, reconcile the answer with Mr. Rothschild's stated recommended range of 7.95 percent to 9.11 percent. If not, explain why his recommended range extends above 8.07 percent.

RESPONSE:

Refer to my direct testimony, page 6, Table 1, which reflects recommended cost rates of 8.50 percent for preferred equity and 8.07 percent for common equity. Refer also to the Application, Direct Testimony of Ann E. Bulkley ("Bulkley Direct Testimony"), page 5, lines 1-9, and page 50, lines 1-5, where Ms. Bulkley recommends a 10.75 percent ROE within a range of 10.25 percent to 11.25 percent.

a. The 8.50% preferred equity cost rate in Table 1 is the cost rate the Company itself assigns to its outstanding preferred stock (Watkins Direct Testimony, page 32, Table 3; Exhibit 37, Schedule J). It is the fixed dividend rate on approximately $2.2 million of preferred stock, representing 0.28% of the Company's capitalization, and it is the same rate carried in the capital structure authorized in Case No. 2025-00122 (Watkins Direct Testimony, page 28, Table 1). It is not a market-based estimate of the return investors currently require on preferred stock. It is included in the capital structure on the same basis as the 4.84% embedded cost of long-term debt: as a contractual cost the Company actually pays, fixed at issuance, not as a measure of current market requirements. My 8.07% recommendation, by contrast, is an estimate of the return investors currently require on common equity, based on current market data. The relative risk and priority of claims between common and preferred equity are reflected in the returns investors require on the two securities at the same point in time. They are not reflected in a comparison between a current market-based return on one security and a contractual dividend rate fixed at issuance on another.

b. Yes. At any given point in time, a rational investor would require a higher expected return on a company's common equity than on its preferred equity, because common equity is subordinate to preferred in its claim on earnings and assets and bears residual risk. My analysis is consistent with that principle: the return investors currently require on utility preferred stock, as reflected in current market yields, is below the 8.07% I recommend for common equity. The 8.50% figure in Table 1 is not a current required return on preferred stock and does not indicate otherwise.

c. The 8.07% ROE remains reasonable because it is a market-based estimate of the current cost of common equity, and the 8.50% figure is the fixed dividend rate on a security representing 0.28% of the Company's capitalization. The two figures measure different things and are not comparable. No, the recommended ROE should not be adjusted to the preferred equity cost rate. Doing so would set the return on common equity by reference to a contractual dividend rate established under past market conditions rather than by reference to the return investors require today, and it would make the authorized ROE depend on the historical financing decisions that happen to remain on the Company's books rather than on current capital market evidence.

d. I consider an ROE within my recommended range of 7.95% to 9.11% reasonable. The portion of the interval between my 8.07% recommendation and Ms. Bulkley's 10.75% recommendation that I consider reasonable is therefore the portion from 8.07% to 9.11%. I do not consider any ROE above 9.11% reasonable for Kentucky American, for the reasons explained in my testimony. Within my recommended range, the factor the Commission should weigh is the one described at pages 10–11: the market-based cost of equity, which my results place at a median of 6.93%, balanced against the principle of gradualism, which supports a measured rather than immediate transition toward that market-based cost. My recommendation of 8.07%, the 85th percentile of my results, reflects my judgment as to the point within the range that best reflects that balance. The range extends above 8.07% because the cost of equity cannot be measured with precision (page 6 of my direct testimony), and presenting a range from the 80th to the 90th percentile of my results gives the Commission the band within which I am confident the Company can attract the capital it needs. That does not alter my recommendation that 8.07% is the most appropriate point within it.

AFFIDAVIT

STATE OF MICHIGAN)

COUNTY OF WAYNE)

John Defever, Senior Regulatory Consultant, being duly sworn, states that his responses in the above referenced case are true and accurate to the best of his knowledge, information and belief.

John Defever

John Defever

Sworn to and subscribed before me on this 10th day of September 2026.

Christine Miller

Notary Public

CHRISTINE MILLER
NOTARY PUBLIC, STATE OF MI
COUNTY OF WAYNE
MY COMMISSION EXPIRES Nov 8, 2028
ACTING IN COUNTY OF Wayne

AFFIDAVIT

STATE OF CONNECTICUT

COUNTY OF FAIRFIELD

AARON L. ROTHSCHILD, being duly sworn, states that his responses in the above referenced case are true and accurate to the best of his knowledge, information, and belief.

Aaron L. Rothschild

VIDA M. ROTHSCHILD NOTARY PUBLIC CONNECTICUT

Sworn to and subscribed before me on this 9th day of September 2026.

Notary Public

VIDA M. ROTHSCHILD
NOTARY PUBLIC
My Commission Expires May 31, 2027