

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 )

COMMISSION STAFF'S THIRD REQUEST FOR INFORMATION TO  
KENTUCKY-AMERICAN WATER COMPANY

Kentucky-American Water Company (Kentucky-American), pursuant to 807 KAR 5:001, is to file with the Commission the original in paper medium and an electronic version of the following information. The information requested is due on or before March 1, 2019. Responses to requests for information in paper medium shall be appropriately bound, tabbed and indexed. Electronic documents shall be in portable document format (PDF), shall be searchable, and shall be appropriately bookmarked.

Each response shall include the name of the witness responsible for responding to the questions related to the information provided. Each response shall be answered under oath or, for representatives of a public or private corporation or a partnership or association or a governmental agency, be accompanied by a signed certification of the preparer or person supervising the preparation of the response on behalf of the entity that the response is true and accurate to the best of that person's knowledge, information, and belief formed after a reasonable inquiry.

Kentucky-American shall make timely amendment to any prior response if it obtains information that indicates that the response was incorrect when made or, though correct when made, is now incorrect in any material respect. For any request to which

Kentucky-American fails or refuses to furnish all or part of the requested information, it shall provide a written explanation of the specific grounds for its failure to completely and precisely respond.

Careful attention should be given to copied material to ensure it is legible. When the requested information has been previously provided in this proceeding in the requested format, reference may be made to the specific location of that information in responding to this request. When applicable, the requested information shall be separately provided for total company operations and jurisdictional operations. When filing a paper containing personal information, Kentucky-American shall, in accordance with 807 KAR 5:001, Section 4(10), encrypt or redact the paper so that personal information cannot be read.

#### Slippage

1. Refer to Kentucky-American's Response to Commission Staff's Second Request for Information (Staff's Second Request), Item 1.a and Item 4.a. Provide revised budget project schedules for the calendar years 2008 through 2017, eliminating the construction projects that were approved by the Capital Investment Management Committee (CIMC), but were not included in Kentucky-American's original construction budgets.

2. Using the revised budget project schedules provided in the response to Item 1. above, provide a schedule that calculates the ten-year average slippage factor for the original construction budgets for calendar years 2008 through 2017.

3. Refer to Kentucky-American's Response to Staff's Second Request, Item 4.a. Kentucky-American provided a schedule that lists each project by year and includes

a description of each project but failed to provide a detailed reason for each project that was constructed but not included in the annual budget, as requested. Resubmit the response and include a detailed reason for each project that was constructed but not included in the annual budget for 2008–2017.

4. Confirm that the construction projects approved by the CIMC, but not included in Kentucky-American’s original construction budgets, are included in Kentucky-American’s Comprehensive Planning Study. If this cannot be confirmed, provide a detailed explanation as to why each project was not included in Kentucky-American’s Comprehensive Planning Study.

5. Refer to Kentucky-American’s Response to Staff’s Second Request, Item 4.a. Provide the Information requested in the schedule below for the calendar years 2008 through 2017.

Item	Budget Projects	Actual Project Cost	Cost Approved by CIMC	Variance in Dollars	Variance Percentage
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6. Provide a schedule that calculates the ten-year average slippage factor for the CIMC construction budgets for calendar years 2008 through 2017.

7. Describe the process for funding approval of Kentucky-American’s construction budgets, including the process for revised funding approval to include construction projects approved by the CIMC but not included in original construction budgets.

8. Explain whether the CIMC receives an expected project schedule with the estimated construction timeline and the construction costs broken down in monthly or yearly time increments when projects are presented to CIMC for approval. If there is a

project schedule with expected time increments, provide the schedule for each project for calendar years 2008 through 2017.

9. State when Kentucky-American revised the construction approval process to include the CIMC review and explain the reason for the formation of the CIMC.

10. Provide copies of all schedules, supporting calculations, and documentation requested in Items 1, 2, 5, and 6 above in Excel spreadsheet format, with formulas intact and unprotected, and all rows and columns fully accessible.

#### Tax Cuts and Jobs Act (TCJA)

11. Refer to Kentucky-American's response to Staff's Second Request, Item 18. State whether Kentucky-American recovered this tax expense through base rates for the period after the Commission's ruling in Administrative Case No. 313<sup>1</sup> and prior to the enactment of the Small Business Jobs Protection Act of 1996.

12. Refer to the Direct Testimony of Melissa Schwarzell (Schwarzell Testimony), page 22, lines 8–10. Ms. Schwarzell explains, "that all new Contribution In Aid of Construction (CIAC) receipts are forecasted to be grossed up for income tax, which offsets the cost of the corresponding tax assets to the general customer base." Explain whether Kentucky-American has "grossed-up" to reflect the Federal Income Taxes (FIT) impact of the TCJA for the CIAC's received after January 1, 2018. If yes, provide a list of CIAC's that have been received, the date the CIAC was received, the cost of the project funded by the CIAC, and the FIT gross-up.

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<sup>1</sup> Administrative Case No. 313, *The Effects of the Tax Reform Act of 1986 on Contributions in Aid of Construction and Customer Advance*, Interim Order (Ky. PSC Apr. 15, 1988).

13. Refer to the Schwarzell Testimony, page 23, lines 4–5. According to Ms. Schwarzell, Kentucky-American began grossing-up customer advances to collect the additional funds from developers to recognize the taxability customer advances received. Provide a list of customer advances that have been received since January 1, 2018, the cost to actually construct each project that was donated to Kentucky-American as a customer advance, and the FIT gross-up for each project.

14. In Administrative Case No. 313, the Commission ordered that taxable Class A and B water and sewer utilities to use the "no gross-up" methodology for CIAC and customer advances collected on and after the date of that Order. Cite any Orders that have been issued by this Commission revising its earlier requirement for Kentucky-American to use that "no gross-up" method.

15. Explain whether Kentucky-American is requesting that the Commission reconsider its ruling in Administrative Case No. 313 requiring Class A and B water utilities to use the "no gross-up" methodology for Contributions in Aid of Construction and Customer Advances.

16. Refer to Kentucky-American's Response to Staff's Second Request, Item 65.b. Kentucky-American refers to its ability to execute a "calculation applying ARAM to all plant related EADIT outside PowerTax using an Excel spreadsheet." Calculate the excess protected and unprotected excess Accumulated Deferred Income Tax (ADIT) using the referenced Excel spreadsheet.

17. If Kentucky-American is unable to provide the Excel spreadsheet requested in Item 16 above, provide an estimated date the spreadsheet will be available. When

available, provide a copy of the Excel spreadsheet with all formulas intact and unprotected, and all rows and columns fully accessible.

18. Refer to Kentucky-American's Response to the Attorney General's First Request for Information (Attorney General's First Request), Item 31.

a. Provide a schedule comparing the protected and unprotected federal excess ADIT reported in Case No. 2018-00042<sup>2</sup> to the amounts to the actual amounts recorded on Kentucky-American's books as a regulatory liability.

b. Explain if the gross-up rate used to record the protected and unprotected federal excess ADIT on Kentucky-American's books use a Kentucky income tax rate of 5 percent or 4 percent.

c. Given that the Kentucky income tax rate change was retroactive to January 1, 2018, confirm that Kentucky-American has recorded the excess State ADIT liability as of the January 1, 2018 effective date.

#### Weather Normalization

19. Refer to Kentucky-American's Response to Staff's Second Request, Item 3. Provide each class's rate of return on rate base and total rate of return on rate base at present and proposed rates.

20. Refer to Kentucky-American's Response to Staff's Second Request, Item 11.

a. Explain why weather normalization is performed in the forecast of water usage.

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<sup>2</sup> Case No. 2018-00042, *Electronic Investigation of the Impact of the Tax Cuts and Job Act on the Rates of Kentucky-American Water Company* (filed Aug. 8, 2018).

b. Explain why Kentucky-American believes the models become insignificant when the climatic component is removed.

c. Provide these regression model results similar to Tables GPR-1 and GPR-2 of the Direct Testimony of Gregory P. Roach (Roach Testimony).

21. Refer to Kentucky-American's Response to Staff's Second Request, Item 26.

a. In the approach to forecasting usage, provide the different independent variables that were used in the regression model and explain why different variables were chosen.

b. Explain why Kentucky-American changed from a cross sectional to a time series model.

22. Refer to the Roach Testimony, page 2, line 20. Provide the data relied on and all calculations used to determine the 987 gallons per residential customer per year trend. State the source for the data provided in Kentucky-American's response.

23. Refer to the Roach Testimony, page 2, line 22. Provide the data relied on and all calculations used to determine the 2,522 gallons per commercial customer per year trend. State the source for the data provided in Kentucky-American's response.

24. Refer to the Roach Testimony, page 5, line 14. Provide the data used to produce figure GPR-1.

25. Refer to the Roach Testimony, page 9, line 9. Provide the data used to produce figure GPR-3.

### Employee Staffing, Compensation, and Benefits

26. Refer to Kentucky-American's Response to Staff's First Request, Item 37, to the responses to Staff's Second Request, Item 27, and to the Direct Testimony of Timothy Willig (Willig Testimony), Page 11. Explain why the actual employee cost share percentage in Schedule 37 for health benefits does not equal the cost share of 24 percent included in the Willig Testimony.

27. Refer to Kentucky-American's Response to Staff's Second Request, Item 31. Explain why Kentucky-American is seeking to recover the cost of its Annual Incentive Plan, given that 50 percent of the corporate multiplier is based on financial performance and that employees will not receive incentive payments if Earning per Share falls below 90 percent of the target.

28. Refer to Kentucky-American's Response to Staff's Second Request, Item 32, which was unresponsive. Confirm that Kentucky-American has not performed or commissioned a study or analysis that quantifies the benefits its ratepayers derive from the Annual or Long-Term Performance Plans.

29. Refer to Kentucky-American's Response to Staff's Second Request, Item 34. Confirm that no specific study was conducted to quantify the benefits the ratepayers derive from the Annual and Long-Term Performance Plans.

30. Refer to Kentucky-American's Response to Staff's Second Request, Item 44. Explain why Kentucky-American is seeking to recover the cost of its incentive programs, on attracting new employees or employee retention, given that no specific studies or analyses on the impact of such incentive programs, have been completed.



31. Refer to Kentucky-American’s Response to Staff’s Second Request, Item 45, and to the Direct Testimony of Kevin Rogers, page 19. Explain why annual work orders in 2018 are projected to increase by 25 percent, to 98,000 from only a 6.8 percent increase the year prior.

32. Refer to Kentucky-American’s Response to the Attorney General’s First Request, Item 8. For each department listed in the table below, provide a detailed explanation for the forecasted increase in employee staffing from the “2014 December Actual” to the “2020 June Forecast.”

<u>Department</u>	2014 December <u>Actual</u>	2020 June <u>Forecast</u>
Production	39	46
Distribution	65	74
Commercial	0	7
Administrative & General	22	25

33. Provide a detailed explanation as to the fluctuation in the commercial department from 0 employees in December 2014, to 24 employees in December 2015, and to 9 employees in December 2016.

Qualified Infrastructure Project (QIP) Rider

34. Refer to the Direct Testimony of Nick O. Rowe (Rowe Testimony), page 11, lines 4–7. Given that this Commission adopted the use of a forecasted test year to reduce regulatory lag and that Kentucky-American has filed forecasted rate cases since 1992, quantify the significant and persistent regulatory lag referred to in Mr. Rowe’s testimony.

35. Refer to the Direct Testimony of Brent E O’Neill P.E. (O’Neill Testimony), page 26, lines 8–11. Mr. O’Neill explains that Kentucky-American has developed detailed plans for the types of projects that will constitute the majority of the work performed under

the first years of the QIP Rider. Provide a detailed list of the projects that would be recovered through the first five years of the proposed QIP Rider. The list should include the projected cost of each project and estimates of the QIP that would be required for each project.

36. Refer to Kentucky-American's Response to Staff's Second Request, Item 49.b. Provide a detailed explanation of the importance of the QIP projects to Kentucky-American's ability to provide safe, adequate, and reliable water service to its ratepayers.

37. Refer to Kentucky-American's Response to Staff's Second Request, Item 53.a. Kentucky-American states that a forecasted QIP would allow the Commission to review all aspects of the filing including the verification that the included projects qualify for the QIP and are prudent. Explain why a historical QIP would not allow the Commission to conduct such a review after the projects were completed.

38. Refer to Kentucky-American's Response to Staff's Second Request, Item 53.a. Explain in detail why a forecasted QIP would act as a greater incentive to ensure Kentucky-American maintains its focus on the replacement of cast iron mains.

39. Refer to Kentucky-American's Response to Staff's Second Request, Item 54. Kentucky-American continues to refer in generalities to the potential cost savings an infrastructure replacement rider, Distribution System Improvement Charge (DSIC), or QIP will provide to its ratepayers.

a. Provide an analysis that quantifies the annual cost savings that Kentucky-American expects to occur in the first five years if the QIP rider is approved.

b. Explain how Kentucky-American would respond to a Commission requirement that approval of the QIP Rider is contingent on Kentucky-American's

commitment to include a provision for any estimated cost savings. Provide a detailed explanation for Kentucky-American's response.

40. Refer to Kentucky-American's Response to Staff's Second Request, Item 55.

a. Kentucky-American was asked to provide detailed estimates of the cost it would incur when it files the annual QIP request in Case No. 2012-00520<sup>3</sup> and in Case No. 2015-00418.<sup>4</sup> Explain why Kentucky-American is not prepared in this instant case to provide the requested cost estimates.

b. Given the number of American Water subsidiaries that have an infrastructure replacement rider, explain why Kentucky-American is unable to use the costs actually incurred by the other subsidiaries as the basis for a cost estimate for its annual QIP request.

41. Refer to Kentucky-American's Response to Staff's Second Request, Item 54.

a. Kentucky-American was requested to provide detailed estimates of the cost it would incur when it files an annual Balancing Adjustment filing in Case No. 2012-00520 and in Case No. 2015-00418. Explain why Kentucky-American is not prepared in this instant case to provide the requested cost estimates.

b. Given the number of American Water subsidiaries that have an infrastructure replacement rider, explain why Kentucky-American is unable to use the

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<sup>3</sup> Case No. 2012-00520, *Application of Kentucky-American Water Company for an Adjustment of Rates Supported by a Fully Forecasted Test Year* (Ky. PSC Oct. 25, 2013).

<sup>4</sup> Case No. 2015-00418, *Application of Kentucky-American Water Company for an Adjustment of Rates* (Ky. PSC Aug. 23, 2016).

costs actually incurred by the other subsidiaries as the basis for a cost estimate for its annual Balancing Adjustment filing.

42. Refer to the O'Neill Testimony, page 24, lines 9–21 and the responses to Staff's Second Request, Item 57. Identify each American Water subsidiary that is authorized to include the replacement of aging treatment plant items or facilities, (i.e., pumping equipment, generators, water quality sampling equipment, SCADA equipment, and treatment equipment) through its infrastructure replacement tariff rider.

43. Refer to Kentucky-American's Response to Staff's Second Request, Item 63.

a. The response states that Kentucky-American would consider extending the interval between filing rate cases if significant issues in this instant case are resolved in a way that will allow Kentucky-American a reasonable opportunity to earn its authorized return. Explain if this response means that granting the requested QIP Rider alone will not affect the time between rate case filings.

b. If approval of the QIP Rider would be contingent on a Kentucky-American commitment to extend the time interval between rate case filings, provide the interval Kentucky-American would commit. Provide a detailed explanation for Kentucky-American's response.

44. If Kentucky-American is unwilling to commit to extending the interval between filing rate cases and continues its current course of submitting rate cases approximately every two years, respond to the following view that Kentucky-American's estimated impact of the accelerated replacement rider has been overstated.

45. In Case No. 2012-00520, KAWC proposed to implement a DSIC that would permit it to accelerate the replacement of aging infrastructure. Provide a comparative analysis listing the similarities and the differences between the DSIC and the proposed QIP Rider in this instant case. Include detailed discussions for each similarity and difference noted in Kentucky-American's comparative analysis.

46. Kentucky-American's proposed DSIC mechanism was denied by the Commission in Case No. 2012-00520. Provide a detailed explanation of what has changed since Case No. 2012-00520 that would persuade the Commission to revise its opinion and to approve the proposed QIP in this instant case.

Service Company

47. Refer to Kentucky-American's Response to Staff's Second Request, Item 70, page 3 of 4. Provide a breakdown for each identified expense category between the costs directly charged and indirectly charged to Kentucky-American. Include descriptions of the services being provided for each listed category.

- a. GL Account 50100000 - Labor Natural Account
- b. GL Account 52567000 - Relocation Expense
- c. GL Account 53110000 - Contract Svc-Eng. – Natural Account
- d. GL Account 53150000 - Contract Svc-Other – Natural Account
- e. GL Account 53151000 - Contract Svc-Temp Empl. – Natural

Account

- f. GL Account 53155000 - Contract Svc-Legal – Natural Account

48. Refer to responses to Staff's Second Request, Item 70, page 4 of 4, Support Services Total Costs. Provide a breakdown of the costs directly and indirectly charged

to Kentucky-American. For each category, include a complete description of the services being provided.

- a. Investor Relations
- b. Legal
- c. Technology and Innovation (T&I)

North Middletown Acquisition

49. Refer to Kentucky-American's Response to the Staff's Second Request, Item 72.

a. In performing its due diligence in the acquisition of North Middletown, explain whether Kentucky-American identified any areas that will require it to make capital investments to maintain or improve North Middletown's facilities. If yes, provide a list of the projects and the estimated cost for each project.

b. Provide a description and quantify the overall benefits (financial and service) that Kentucky-American's existing customer base received in the acquisition of North Middleton.

50. Fair market value (FMV) is defined as the amount for which property would sell on the open market if put up for sale in the ordinary course of business and that FMV is usually determined by the purchase price of similar goods or property in the same locality.<sup>5</sup> Explain how the purchase price paid by Kentucky-American for a facility it acquires would constitute the FMV without considering the purchase price of similar utility assets in the same general area.

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<sup>5</sup> U.S. Legal, *Fair Market Value Law and Legal Definition*, <https://definitions.uslegal.com/f/fair-market-value/>.

51. Provide a copy of any appraisals that were performed in connection with the proposed acquisition of North Middletown's facilities.

52. Refer to Kentucky-American's Response to the Staff's Second Request, Item 74.

a. Explain how the elimination of the "Delta Test" would ensure that there are reasonable negotiations between the parties if whatever a utility is allowed to recover in rates is whatever the utility actually pays for an acquisition.

b. The Uniform System of Accounts for gas utilities states, "The gas plant accounts shall not include the cost or other value of gas plant contributed to the company. Contributions in the form of money or its equivalent toward the construction of gas plant shall be credited to the accounts charged with the cost of such construction." Given that the utility plant values listed for each gas utility is net of contributions, explain the relevance and the reliability of Kentucky-American's comparative schedule.

#### Non-Recurring Charges

53. Refer to Kentucky-American's Response to Staff's Second Request, Item 16.

a. Explain how Kentucky-American calculated the total residential service cost for 3/4-inch meters for calendar years 2012–2017. Provide all workpapers and calculations and state all assumptions that show how the total cost was calculated.

b. Refer to the chart at the top of the page titled "Account 12002002 – 5/8" & 3/4" Meter Installations (Settings)." Explain how this chart is used in developing the proposed tap fees.

c. Provide verification and/or invoices for the costs of the 5/8", 1" and 2" meters supplied by Badger Meter Company.

Cost of Service Study (COSS)

54. Refer to Kentucky-American's Response to Staff's Second Request, Item 76. Ms. Heppenstall corrected her testimony stating that the estimated demands were based on the demand factors reflected from the Customer Class Water Demand Study-1999 performed by Burgess and Niple. Given that this study is almost ten-years old, explain whether Kentucky-American believes the results are still applicable today given efficiency and conservation efforts.

Return on Equity (ROE)

55. The Federal Reserve recently signaled that they were not going to increase interest rates in March 2019.<sup>6</sup> Explain if this affects Kentucky-American's ROE analysis.

56. Refer to Kentucky-American's Response to Staff's Second Request, Item 87b. Ms. Buckley states that Kentucky-American's proposed ROE of 10.80 percent is with the assumption that the proposed QIP is approved. Explain what ROE Kentucky-American proposes if the proposed QIP is not approved and provide support for this proposed ROE. Calculate the revenue requirement impact the revised ROE would have.

57. Refer to Kentucky-American's Response to Staff's Second Request, Item 92. Provide an explanation for the decline in Kentucky-American's earned ROE beginning in August 2018.

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<sup>6</sup> <https://www.nytimes.com/2019/01/09/business/economy/fed-interest-rates-minutes.html>



## Capital Structure

58. Refer to Kentucky-American's Response to the Attorney General's First Request for Information, Item 48. Since 2010, the percent of common equity to total capital has increased from less than 45 percent to almost 47.5 percent. Also, refer to the application, the Direct Testimony of Scott W. Rungren, Exhibit SWR-1. Here the forecasted percent of common increased to 48.7. Provide an explanation for the increase in the ratio of common equity to total capital.



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DATED FEB 13 2019

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