

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

RECEIVED

In the Matter of:

APPLICATION OF AUXIER WATER
COMPANY, INC. FOR AUTHORIZATION OF
ITS PROPOSED SALE AND CONVEYANCE
OF ALL OF ITS WATER DISTRIBUTION
SYSTEM AND CUSTOMER DEPOSITS TO
THE CITY OF PRESTONSBURG,
KENTUCKY

JAN 24 2008

**PUBLIC SERVICE
COMMISSION**

CASE NO. 2007-00488

**AUXIER WATER COMPANY'S
RESPONSES TO COMMISSION STAFF'S FIRST DATA REQUEST**

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WATER COMPANY, INC.

January 24, 2008

REQUEST:

1. For its water distribution system and customer deposits, Auxier will receive \$2,650,000 and other valuation consideration, including commitments of Prestonsburg respecting water service in Auxier's service territory.¹

- a. Explain the term "other valuation consideration."
- b. Describe the water service commitments that Auxier will receive.

RESPONSE:

1. a. The "other valuable consideration" consists of the obligations of the City pursuant to Section 302 of the Acquisition Contract. *See also* Response of Prestonsburg to Staff's First Data Request No. 1.

1. b. Auxier will not receive any "water service commitments." The Application term states: "including certain commitments of the City respecting water service in Applicant's service territory." The commitments referred to go not to Auxier, but to the City's obligation to supply water service in Auxier's service territory. The obligation is included at Section 302(5) of the Acquisition Agreement. *See also* Response of Prestonsburg to Staff's First Data Request No. 1.

¹ Application at 2.

REQUEST:

2. KRS 278.020(6) provides that the Commission must find that the proposed transaction “[i]s to be made in accordance with law, for a proper purpose and is consistent with the public interest.” Explain how the proposed transaction benefits the public.

RESPONSE:

2. The proposed transaction benefits the public in many ways. First, by Auxier’s customers being served by the City, they will have the additional service protection of a larger utility with more equipment and assets to meet their water supply needs. Specifically, Auxier currently has a staff of four (4) people – two (2) of whom perform field work (Phil Ward and Victor Goble). Mr. Ward, 58 years old, is one of the owners of Auxier, and he dedicates an enormous amount of time and commitment to meet the needs of Auxier’s customers. If he were to become ill or incapacitated, Auxier and its customers would face a severe situation. This potential risk would be alleviated through the sale to the City.

Second, the public would benefit by achieving a level of retail water rate stability, and probably lower retail water rates in the future, as a result of the sale. Currently, Auxier purchases water from the City at eight (8) different metering points, and Auxier pays the City’s regular rates for water at those points. Accordingly, the additional distribution and management costs of Auxier have to be added on to the water purchase costs and recovered from Auxier’s water customers. Under the Acquisition Agreement, Section 302(5), the City agrees not to increase Auxier’s retail rates unless and until the City’s “Outside Water Rates” to all other customers increases beyond Auxier’s retail rates (they currently are lower). This arrangement is to continue until the Acquisition Debt is paid off by the City, at which time Auxier’s retail water rates will be subject to the “Outside Water Rates,” which means that Auxier’s customers will receive water at the same rate as the City’s numerous other “outside” customers, which rates will likely be lower than currently being charged by Auxier. And, should the Auxier area ever be annexed into the City, Auxier’s customers will benefit from the lower Inside Rates.

In this regard, if there were no sale to the City, Auxier would have to incur additional personnel costs (because of the stress and risk currently being carried by Mr. Ward), and would otherwise have to seek a purchased water adjustment and a retail rate increase (rates have not been increased since 1986). Thus, the Acquisition Agreement would avoid rate increases that would be forthcoming very shortly, and since the Acquisition Agreement would obviate the need for such an increase, the public would be benefited.

Additionally, the City’s water system is excellent; it is recognized as being one of the truly superior municipal systems in the region. Auxier’s customers would benefit by being served by such an excellent utility.

Finally, the proposed sale is consistent with public interest as recognized in KRS 224.310 and in KRS 74.361 (applicable to water districts):

WITNESS: Philip Ward

The General Assembly of the Commonwealth of Kentucky determines as a legislative finding of fact that reduction of the number of operating water districts in the Commonwealth will be in the public interest, in that mergers of such districts will tend to eliminate wasteful duplication of costs and efforts, result in a sounder and more businesslike degree of management, and ultimately result in greater economies, less cost, and a higher degree of service to the general public; and that the public policy favors the merger of water districts wherever feasible.

See also Response of Prestonsburg to Staff's First Data Request No. 2.

REQUEST:

3. According to the Acquisition Contract dated September 24, 2007, Auxier will “deliver to the City and its Utilities Commission (a) all sums of money which it then holds, representing deposits made by Auxier’s water users as security for the payment of water bills.”²

a. Identify the amount of the customer deposit liability that Auxier has outstanding as of December 31, 2007 that will be transferred to Prestonsburg.

b. Identify any of Auxier’s outstanding customer deposit liabilities that will be refunded to customers prior to the proposed transfer.

RESPONSE:

3. a. The amount of customer deposits held by Auxier as of December 31, 2007 was \$30,770. This amount, as adjusted for additional deposits and refunds made subsequent to December 31, 2007, will be transferred to Prestonsburg at closing.

3. b. Auxier will refund a deposit to any customer terminating service prior to closing at the time the customer terminates service.

² Acquisition Contract at 6.

WITNESS: Philip Ward

REQUEST:

4. Commission regulations require that interest be paid on customer deposits annually. Auxier's annual report to the Commission for the Calendar Year Ending December 31, 2006 indicates that Auxier did not accrue interest on its customer deposits. Provide the amount of accrued interest on customer deposits Auxier owes as of December 31, 2007.

RESPONSE:

4. Auxier's financial statements are done on a cash basis, and not an accrual basis; therefore, there is no entry in the financial statements for the accrual of interest. Interest on 2007 deposits in the amount of \$1,846.20 will be credited on the February bill of those Auxier customers with deposits being held by Auxier.

REQUEST:

5. The Acquisition Contract states that the future accrual of interest on Auxier's customer deposits will conform to, "[w]hatever policies and practices the City has established."³

a. Describe the policies and practices Prestonsburg has regarding the accrual and payment of interest on customer deposits.

b. Describe the differences between Prestonsburg's policies regarding interest on customer deposits with the requirements contained in Commission regulations.

RESPONSE:

5. a. Prestonsburg does not accrue or pay interest on customer deposits.

5. b. The Commission regulation, 807 KAR 5:006, Section 7(6), requires interest on customer deposits to be paid annually to the customers/depositors. The City does not have a parallel requirement (see Response 5(a) above).

³ Id.

REQUEST:

6. Provide the proposed journal entry that Auxier will use to record the transfer.

RESPONSE:

6. The following journal entries will be employed on the books of Auxier to record the transfer, as follows:

ACCOUNT NAME	DEBIT	CREDIT	
CASH	2,584,767.59		(1)
NOTE PAYABLE – CTB LOC	34,462.41		(1)
CUSTOMER DEPOSITS	30,770.00		(1)
MAINS		837,518.73	
METERS		104,802.70	
HYDRANTS		8,300.00	
ACCUMULATED DEPRECIATION	488,607.94		
GAIN ON TRANSFER OF ASSETS		2,187,986.51	
TOTAL DEBITS AND CREDITS	3,138,607.94	3,138,607.94	

(1) REPRESENTS TOTAL SALE PRICE OF \$2,650,000.00.

WITNESS: Philip Ward

REQUEST:

7. Provide the proposed journal entry that Prestonsburg will use to record the transfer.

RESPONSE:

7. *See Prestonsburg's Response to Staff's First Data Request, No. 7.*

REQUEST:

8. Exhibit B of the application is the Report on Audit of Financial Statement for the years ended June 30, 2006 and 2005 for the Prestonsburg City Utilities Commission. Provide a copy of the Water Division's balance sheet, income statement, and statement of retained earnings for the 12-month period ending December 31, 2007.

RESPONSE:

8. *See Prestonsburg's Response to Staff's First Data Request, No. 8.*

REQUEST:

9. Provide a copy of Auxier's balance sheet, income statement, and statement of retained earnings for the 12-month period ending December 31, 2007.

RESPONSE:

9. A copy of Auxier's balance sheet, income statement, and statement of retained earnings for the 12-month period ending December 31, 2007 is attached as hereto as Exhibit 1.
(The level of retained earnings is reflected on the balance sheet.)

WITNESS: Philip Ward

REQUEST:

10. Identify the Prestonsburg employees who will manage and operate Auxier's water system and describe each person's qualifications to operate and manage a water distribution system.

RESPONSE:

10. *See* Prestonsburg's Response to Staff's First Data Request, No. 10.

REQUEST:

11. a. Describe the internal standards and policies of Prestonsburg regarding service reliability and quality of its water utility operations.
- b. Provide all written standards or policies related to service quality and reliability of water utility operations.

RESPONSE:

11. a. *See* Prestonsburg's Response to Staff's First Data Request, No. 11.
11. b. *See* Prestonsburg's Response to Staff's First Data Request, No. 11.

REQUEST:

12. Provide in table format an analysis of the number and type of consumer complaints that Prestonsburg received during the period from 2000 to 2005 and of how such complaints were resolved.

RESPONSE:

12. *See Prestonsburg's Response to Staff's First Data Request, No. 12.*

REQUEST:

13. a. List all of Auxier's current employees.
- b. Identify each Auxier employee that Prestonsburg will not retain after the acquisition is completed, explain why he or she will not be retained, and describe the severance package, if any, that he or she will receive.
- c. Provide the job duties and salary of each Auxier employee to be hired by Prestonsburg.
- d. Will the hiring of any Auxier employee fill a current vacancy at Prestonsburg? If yes, state the current vacant position and how long that position has been vacant.
- e. Who will supervise the Auxier employees hired by Prestonsburg?

RESPONSE:

- a. The following are Auxier's current employees:
 - (i) Philip Ward
 - (ii) Pat Music, part-time employee
 - (iii) Victor Goble
 - (iv) Cheryl Williams
- b. No employee will be hired or retained by Prestonsburg because the City currently has adequate staffing to handle the Auxier work. Mr. Ward will continue to conduct his construction business, and Mr. Goble will become an employee of that business. Ms. Music will be retiring (she is eligible for social security). No employee will receive a severance package.
- c. Not applicable.
- d. Not applicable.
- e. Not applicable.

WITNESS: Philip Ward

AUXIER WATER COMPANY, INC.
BALANCE SHEET
December 31, 2007

ASSETS

CURRENT ASSETS

Petty Cash	\$	00.00
Citizen's		51,505.84
Cash on Hand		100.00
Citizen's Nat'l - M/D		38,240.51
Accounts Receivable		<u>42,880.63</u>

Total Current Assets 130,825.07

PROPERTY AND EQUIPMENT

Utility Plant	999,471.02
Machinery & Equipment	124,958.63
Accumulated Depreciation	<u>(628,058.73)</u>

Net Property and Equipment 496,370.92

TOTAL ASSETS \$ 627,195.99

AUXIER WATER COMPANY, INC.
BALANCE SHEET
December 31, 2007

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES		
N/P - Forest Music	\$	13,375.18
N/P - Philip Ward		24,285.18
A/P - H2O Daniel's Creek		85,139.81
Accounts Payable		17,670.22
A/P H2O Construction Corp		5,079.75
Accrued Interest S/H		61,322.10
Customer Deposits		30,770.00
Accrued Fica/Fed/Medi		2,815.18
Accrued KWT		482.82
Accrued KUI		2.07
Accrued Johnson County WTH		17.10
Accrued Sales Tax		174.37
Accrued John. County School Tax		395.79
Accrued Interest		<u>1,846.20</u>
Total Current Liabilities		<u>243,375.75</u>
LONG-TERM LIABILITIES		
N/P - CTB LOC		<u>34,462.41</u>
Total Long-Term Liabilities		<u>34,462.41</u>
Total Liabilities		<u>277,838.16</u>
STOCKHOLDERS' EQUITY		
Capital Stock		3,088.00
Retained Earnings		118,571.45
Contributed Capital		184,973.40
Current Earnings		<u>42,724.08</u>
Total Stockholders' Equity		<u>349,357.83</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$	<u><u>627,195.99</u></u>

**AUXIER WATER COMPANY, INC.
INCOME STATEMENT**

**12 Months Ended
December 31, 2007**

Int. Expense - F. Music	(1,337.52)
Int. Expense - P. Ward	<u>(2,428.52)</u>
Total Other Income (Expense)	<u>(9,094.02)</u>
Net Income (Loss) Before Taxes	<u>42,724.98</u>
Net Income (Loss)	<u>\$ 42,724.98</u>

**AUXIER WATER COMPANY, INC.
INCOME STATEMENT**

12 Months Ended
December 31, 2007

Sales	
Water Sales - Residential	\$ 454,577.93
Water Sales - Commercial	52,132.17
Service Fee & Penalties	12,446.70
Miscellaneous Income	11,781.83
Less Returns & Allowances	<u>0.00</u>
Total Sales	<u>530,938.63</u>
Gross Profit	<u>530,938.63</u>
Operating Expenses	
Salaries and Wages	68,077.74
Salaries - Officers	54,737.40
Employee Pens. & Benefits	1,172.25
Water Purchases - P'burg	190,039.57
Employee Pensions & Benefits	1,267.80
Office Supply & Other Expense	6,022.02
Oper. Supp. & Exp. T & D	14,727.37
Telephone & Utilities - Office	5,932.92
Bank Charges	181.81
Contractual Services/Consulting Fees	30.00
Accounting	12,975.00
Legal	2,895.52
Contract Labor	1,567.00
Rents	19,200.00
Transportation Expenses	10,281.38
Property Insurance	1,206.00
Worker's Compensation	2,481.77
Officer's Life Insurance	2,676.00
Employee Benefits	12,678.00
Insurance	11,615.89
DUES AND SUBSCRIPTION	395.00
Bad Debt Expense	780.55
Miscellaneous Expenses	1,805.37
Depreciation Expense	34,820.89
Payroll and Other Taxes	9,880.64
PSC Assessment	10,388.54
Misc. Tax & Licenses	<u>1,185.00</u>
Total Operating Expenses	<u>479,119.63</u>
Operating Income (Loss)	<u>51,819.00</u>
Other Income (Expense)	
Interest Income	257.73
Interest Expense - LOC	(3,739.51)
Interest Expense - Meter Deposit	(1,846.20)