

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE TARIFF APPLICATION OF KENTUCKY-)
AMERICAN WATER COMPANY PROCEDURE FOR) CASE NO.
COMPUTING REVENUE REQUIREMENTS) 10423

O R D E R

IT IS ORDERED that Kentucky-American Water Company ("Kentucky-American") shall file an original and 12 copies of the following information with the Commission with a copy to all parties of record no later than December 7, 1988. If the information cannot be provided by this date, Kentucky-American should submit a motion for an extension of time stating the reason a delay is necessary and include a date by which it will be furnished. Such motion will be considered by the Commission. Kentucky-American shall furnish with each response the name of the witness who will be available at the public hearing for responding to questions concerning each item of information requested.

1. On September 30, 1988 Kentucky-American supplied the Commission with the following projections: (1) the cost of constructing the 30 inch raw water line and the Kentucky River Station No. II; and (2) Kentucky-American's proposed plan of financing the two projects. The following questions are in reference to those projections:

a. Separately identify all projected investment, financing, revenues, and expenses for each construction project

described above. In support of the projections provide all assumptions, calculations, and working-papers for the years 1988, 1989, 1990 and 1991.

b. On Page three of the Application, Kentucky-American stated that the bids received thus far are less than its original cost projections. Provide a detailed list showing the original projected cost, the actual bids received, and the difference.

c. Have the bids received thus far resulted in revisions to Kentucky-American's original projections? If so, provide any revised projection and include supporting documentation.

2. Kentucky-American has proposed to finance the construction projects with two separate phases of financing. The Initial Phase consists of \$12,000,000 debt and \$8,000,000 common stock, and the Second Phase has \$13,000,000 debt and \$7,000,000 common stock. The following questions are in reference to Kentucky-American's proposed financing plans:

a. Kentucky-American's Initial Phase of financing has a debt/common stock ratio of 60/40, with the Second Phase having a ratio of 65/35. Explain the criteria Kentucky-American used to determine the appropriate debt/stock ratios.

b. Provide projected interest rates for the two separate debt issuances, along with supporting documentation.

c. If the closing date of the financing is different than the construction completion date, will the result be an imbalance between net investment rate base ("rate base") and

capital structure? What effect, if any, would this have on either the step increase or a general rate case?

d. If the financing is invested in short-term investments until required to pay construction costs, will this result in an adjustment to Kentucky-American's revenue requirement based on the short-term interest income. How is this reflected in budgeted figures? Identify the amounts.

e. Will Phase I of Kentucky-American's financing be included in the general rate case expected to be filed January 1989? If not then, when and how will it be included in Kentucky-American's capital structure?

f. If the bids are lower than anticipated, will this affect the proposed financing plan?

g. If financing is greater than the final construction cost, how will the remaining funds be utilized and how does Kentucky-American propose to reflect this in the step increase?

3. Provide Kentucky-American's yearly budget forecasts for the period affected by the construction projects and related financing. Include both projected customer growth and water sales in gallons as well as any decreased expenses resulting from the new construction. Identify all assumptions used in these projections and provide all working papers.

4. Provide monthly cash flow projections for the period affected by Kentucky-American's proposed step increase plan. Kentucky-American should separately show cash flows based on including and excluding the step increases. Identify all

assumptions used in these projections and provide all working papers.

5. In lieu of step increases, has Kentucky-American considered using a future test period? If so, provide the reasons for excluding it from the viable alternatives; if not, provide your opinion and understanding of the concept and how it could be used instead of step increases.

6. Provide all analyses Kentucky-American used to determine its proposed use of step increases. Provide a narrative description of all alternatives considered including supporting workpapers, etc.

7. Based on Kentucky-American's capital structure as of October 31, 1988 and the methodology used in determining the appropriate capital structure and overall rate of return in Case No. 10069, Notice of Adjustment of the Rates of Kentucky-American Water Company, issued on June 3, 1988, project the effect that the proposed financing would have on Kentucky-American's capital structure and overall rate of return. Include documentation supporting the calculations.

8. Kentucky-American estimated that the combined cost of a general rate case for all parties concerned would be \$300,000. The following questions are in reference to rate case cost:

a. Provide an estimate of the expected cost of the rate case to be filed in January 1989. Provide all associated workpapers and assumptions.

b. Provide the estimated future savings that Kentucky-American could expect to achieve if the step rate tariff is approved. Provide all associated work papers and assumptions.

9. In order to substantiate the accuracy of the proposed rates, Kentucky-American proposed to file a billing analysis detailing usage for a specified 12-month period. The following questions are in reference to Kentucky-American's proposed billing analysis form:

a. Would the billing analysis include the actual 12-month usage and customers or will it be an annualization of the end-of period customers and usage?

b. If an annualization is used what methodology would Kentucky-American use (i.e., annualize the last month, last quarter...)?

c. If the billing analysis is an actual 12-month period rather than an annualization, would Kentucky-American over earn if the customer count at the end-of-period is greater than the 12-month average?

d. Will the billing information include projected customer and sales growth anticipated from the particular construction? If so, what method will be used for such projections?

10. On page 3 of the Application Kentucky-American states that at the time the new rates are put into effect, it will no longer book an Allowance for the Funds used During Construction ("AFUDC") for the 30 inch raw water line. The following are in reference to AFUDC:

a. What effect would the discontinuance of booking AFUDC have on the Commission's treatment of AFUDC for rate-making purposes?

b. Since AFUDC is currently taxable, will the discontinuance of booking AFUDC for rate-making purposes result in a further difference between rate-making, book, and actual tax expense?

c. If the answer to (b) is yes, what would be the magnitude of the difference on both rate base and deferred income taxes? Provide all workpapers and assumptions.

d. Would this require that the construction completed on the raw water line be excluded from Construction Work in Progress ("CWIP") in the general rate case to be filed January 1989?

11. Will the proposed tariff include any adjustments other than those associated with construction projects?

12. Would Kentucky-American be willing to file monthly status reports on the construction including projected completion dates and over and under runs both in time and costs?

13. The following questions are in reference to Exhibit A of the Application:

a. Provide all workpapers and assumptions used to arrive at Exhibit A.

b. Would property taxes for the period in question reflect taxes associated with CWIP?

c. Is the 20 inch water line cost of \$453,710 net of accumulated depreciation or the original cost?

d. Is accumulated depreciation adjusted to reflect depreciation on the 30 inch raw line?

14. The following questions are in reference to Original Sheets No. 59 and 60 attached to the Application:

a. Provide all workpapers and assumptions used to arrive at Original Sheet No. 60.

b. Is the weighted cost of debt the cost used in Case No. 10069 or is it the expected project cost? If a project cost provide all workpapers and assumptions used to arrive at this projection.

c. Considering that the step increase is associated with a specific construction project and financing, in calculating the weighted cost of debt would it be correct to use the cost of debt from the specific financing phase or the average debt cost determined in the last general rate?

15. Would Kentucky-American be willing to submit the revenue generated from the step rates to an absorption test based on the most current 12-month actual operations being afforded the same rate-making treatment as that used in its last general rate case? If Kentucky-American objects, explain why?

16. If in the general rate case that Kentucky-American files at the close of the construction projects, the Commission determines that Kentucky-American has over-earned, from what period of time should potential refunds be calculated?

Done at Frankfort, Kentucky this 28th day of November, 1988.

PUBLIC SERVICE COMMISSION

Richard D. Henman Jr.
For The Commission

ATTEST:

Executive Director
