

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF WATER SERVICE )  
CORPORATION OF KENTUCKY FOR AN ) CASE NO. 2005-00325  
ADJUSTMENT OF RATES )

COMMISSION STAFF'S SECOND INFORMATION REQUEST  
TO WATER SERVICE CORPORATION OF KENTUCKY

Water Service Corporation of Kentucky ("Water Service") is requested, pursuant to 807 KAR 5:001, to file with the Commission no later than January 31, 2006, the original and 8 copies of the following information, with a copy to all parties of record. Each copy of the data requested should be placed in a bound volume with each item tabbed. When a number of sheets are required for an item, each sheet should be appropriately indexed, for example, Item 1(a), Sheet 2 of 6. Include with each response the name of the witness who will be responsible for responding to questions relating to the information provided. Careful attention should be given to copied material to ensure that it is legible. Where information requested herein has been provided, in the format requested herein, reference may be made to the specific location of said information in responding to this information request.

1. List each case before any state public utility regulatory commissions in which Kristen E. Weeks has testified and describe the subject matter of her testimony in that case.

2. State whether Ms. Weeks conducted a review of Kentucky statutory and decisional law on rate-making practices prior to the filing of her written testimony. If Ms. Weeks conducted such review, describe the nature and extent of this review.

3. At pages 7 and 8 of her testimony, Ms. Ahern quotes *Value Line Investment Survey* (“*Value Line*”) on the ability of large water companies to withstand the burden of increasing costs associated with an aging infrastructure and the threat of bioterrorism. *Value Line* describes how larger companies are acquiring smaller ones that are unable to deal with the financial pressures, and focuses on Aqua America, the largest water utility in its survey and one that offers the highest return on equity of the stocks in the water industry. Explain the connection between acquisitions and the return on equity of a water company. Provide all workpapers, sources, and written materials used to develop the response.

4. At page 8 of her testimony, Ms. Ahern states that the water industry is much more capital-intensive than the electric, natural gas or telephone industries.

a. List all sources and materials that Ms. Ahern relied upon for this statement.

b. Provide all workpapers and written materials Ms. Ahern relied upon for her statement.

c. State Ms. Ahern’s opinion as to how much more capital-intensive the water industry is compared to:

(1) The Electric Industry.

(2) The Telephone Industry.

(3) The Natural Gas Industry.

5. At page 9 of her testimony, Ms. Ahern states that the water utility industry faces a need for increased funds to finance the increasing security costs required to protect the water supply and infrastructure after September 11, 2001. Describe all specific security related projects that Water Services has undertaken since September 11, 2001 and state the dollar amount of those expenditures.

6. At page 14 of her testimony, Ms. Ahern describes her criteria for selecting the proxy companies. The third criterion is that the company must have more than 70 percent of the 2004 operating revenues derived from water operations. Explain why 70 percent was chosen.

7. Refer to page 15 of the Ahern Testimony and PMA-3. PMA-3 is described as containing data for the period 2000-2004. Explain why Ms. Ahern chose this time period.

8. Refer to pages 14 and 15 of the Ahern Testimony and PMA-3 and PMA-4. Both of the proxy groups, the six water companies from AUS Utility Reports and the three water companies from Value Line, include American States Water Co., Aqua America, Inc. and California Water Service Group.

a. State the purpose of developing and using two proxy groups that contain three of the same companies.

b. State whether, since Ms. Ahern believes that Water Services is a small company and should qualify for a small company premium, she considered using the water utility companies in Value Line's Small and Mid-Cap Edition, rather than the large cap water utility companies in the Investment Survey. Explain why.

9. Refer to page 21 of the Ahern Testimony, footnote 10. Provide a copy of the referenced pages.

10. Refer to page 22 of the Ahern Testimony, footnote 11. Provide a copy of the referenced pages.

11. Refer to page 31 of the Ahern Testimony. Explain why Ms. Ahern chose June 20, 2005 as the spot date to calculate an average for the dividend yield.

12. Refer to page 42 of the Ahern Testimony.

a. Explain why Ms. Ahern average three months of data to derive her market equity risk premium.

b. Explain why the three months of data was then averaged with a spot market price from June 17, 2005.

c. Explain why Ms. Ahern chose June 17, 2005 as the spot price.

13. Refer to PMA-1, pages 3, 4 and 15.

a. Footnote 11 on page 4 indicates that the size premium displayed on page 3 for the Proxy Group of Three Value Line Water Companies should be from the sixth decile of the NYSE/AMEX/NASDAQ as shown on page 15. Table 7-5 on page 15, however, indicates that the sixth decile size premium is 1.75 percent, rather than 1.61 percent. Explain the discrepancy and provide any corrected workpapers.

b. State whether Ms. Ahern is stating that the size premium should be between 442 and 480 basis point, but is recommending only 60 and 65 basis points as the adjustment.

c. Describe how Ms. Ahern developed her estimates of 60 and 65 basis points.

14. At page 60, Table 4, of her testimony, Ms. Ahern presents the results of her four models and states that the Indicated Common Equity Cost Rate Before Business Risk

Adjustment is 10.7 percent for the AUS proxy group and 10.9 percent for the Value Line proxy group. Explain how Ms. Ahern developed the percentages.

15. Refer to Exhibit 4 of the Application, Schedule B, Income Statement and w/p(c), Revised Allocations.

a. The first column in the pro forma income statement is the restated test-period operations. Provide a revised pro forma income statement using Microsoft Excel 97 format ("Excel") that includes the columns for the actual test-period operations and the restatement adjustments.

b. Provide a copy of the revised pro forma income statement requested in 15(a) on a computer disk.

c. The restatement adjustments listed on w/p(c) are by expense sub-accounts, but the restatement adjustments that will be included on revised pro forma income statement requested in 15(a) will be by major expense accounts. Provide a schedule reconciling the restatement adjustments on w/p (c) with the adjustments on the revised pro forma income statement requested in 15(a).

d. For each restatement adjustment shown on w/p(c), provide the allocation factor that was used and the calculation of the restatement adjustment.

16. In response to Question 14 of her direct testimony, Kirsten E. Weeks states that "[a]ll other maintenance and general expenses were adjusted by 5.518 percent to account for the increase in the consumer price index since acquisition."

a. Explain the phrase "[t]o account for the increase in the consumer price index since acquisition."

b. Administrative Regulation 807 KAR 5:001, Section 10(7), provides that, “[u]pon good cause shown, a utility may request pro forma adjustments for known and measurable changes to ensure fair, just and reasonable rates based on the historical test period.” Explain how an inflationary expense adjustment based upon a consumer price index is a known and measurable change.

17. Refer to Water Services response to Commission Staff’s First Data Request, Items 12 and 18.

a. Provide an employee schedule in the format provided in Schedule 17 in Excel. Include a copy of the employee schedule on a computer disk.

b. In calendar year 2004 Water Service capitalized \$125,579 of employee salaries, benefits, and payroll taxes. Explain how Water Service calculated the amount that was capitalized in 2004. Provide a breakdown of the \$125,579 between the three components.

c. Provide the percentage wage increases that were granted in calendar year 2003 by employee.

18. Refer to the Revised w/p(b), Calculation of Salary and Benefits, that was filed December 21, 2005.

a. Provide a detailed calculation of each salary listed in the column “Total Annualized Salary.”

b. Explain in detail how the 2004 employee health insurance premium of \$4,332 was derived.

c. Provide a comparison of the 2003, 2004, 2005, and 2006 employee health insurance premiums.

d. In response to 12(b) of the Commission Staff's First Data Request, Water Service provided its Employee Manual. According to the Employee Manual, the employee is responsible for a portion of the premiums for the health and dental insurance coverages. State whether the 2004 employee health insurance premium of \$4,332 exclude, the amount of the premium that the employee paid.

e. Provide the gross amount of the insurance premium for each employee listed, the amount of the premium that was paid by each employee, and how the employee portion of the premium was calculated.

f. Provide a complete description of the "WSC Salary Allocation, including bonus" of \$29,306. Separate the amount between the salary and the bonus, with an explanation of the purpose of the bonus. Identify the expense account that the \$29,306 was allocated.

g. According to the w/p(b), "Salaries at the WSC level were increased by \$70,000 to account for two new hires in HR." Identify the amount allocated to Water Service for the new HR hires and the expense account in which it is recorded. State the date the positions were filed and new employees actual salaries.

19. In response to question 14 of her direct testimony, Ms. Weeks states that, "[s]alaries and wages for operators and office personnel were adjusted by 4 percent to reflect the anticipated raises for employees." However, the rate at the bottom of Revised w/p(b), Calculation of Salary and Benefits, states the salaries include adjustments of 3.5 percent. Explain the discrepancy between the two statements.

20. According to the revised w/p(b-2), Calculation of Pro Forma Operating Expenses Charged to Plant, the amount of operating expenses charged to plant in 2004

was \$121,266. However, in its response to Commission Staff's First Data Request, Item 12(a), Water Service states that in 2004 the capitalized amount was \$125,579. Explain the discrepancy between the two statements.

21. In response to Question 16 of her direct testimony, Ms. Weeks states that in recalculating accumulated depreciation a composite rate of 2 percent was used for water plant and a 25 percent depreciation rate was used for computer and transportation equipment. In its filing of November 3, 2005, Water Service provided "[t]he appropriate useful lives for classes of plant accounts."

a. Recalculate accumulated depreciation, depreciation expense, amortization of CIAC and AIAC, and deferred income taxes using the depreciation lives filed on November, 3, 2004.

b. Determine the effect of the revisions requested in Item 21(a) on Water Service's pro forma operations, rate base, and revenue requirement.

c. Provide copies of all workpapers, calculations, and assumptions used in the responses to 21(a) and 21(b).

22. In response to Question 16 of her direct testimony, Ms. Weeks states that, "[t]he rate filing also includes \$36,282.69 of organizational costs in utility plant in service that was not booked at the time of acquisition." State the purpose of the organizational costs, why they were not booked at the time of acquisition, and why they should be included in Water Service's rate base.

23. In response to Question 15 of her direct testimony, Ms. Weeks states that Water Service has invested nearly \$1,000,000 in utility plant in service since acquisition.



However, in Case No. 2005-00433,<sup>1</sup> Water Service states that “Utilities has infused over \$200,000 to fund over 40 capital projects undertaken and completed by Water Service during the short time that Water Service has owned and operated the Kentucky facilities.” Explain the discrepancy between these statements.

24. In response to Question 16 of her direct testimony, Ms. Weeks explains the column entitled “Per Restatement” on Schedule C. Identify the assets that are now being recorded, the date they were placed into service, and explain why they were not originally recorded by Water Service.

25. Refer to Exhibit 10 of the Application, Schedule C, Rate Base and Rate of Return.

a. The first column in the rate base is entitled “Per Restatement.” Provide a revised pro forma income statement using Excel that includes the columns for the actual test-period operations and the restatement adjustments.

b. Provide a copy of the revised rate base requested in 25(a) on a computer disk.

c. Accumulated depreciation, CIAC, and AIAC has been restated to reflect a 2 percent depreciation rate from the date the assets were placed in service. State the effect of these adjustments on deferred income taxes. State all assumptions, show all calculations, and provide all workpapers used to determine these effects.

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<sup>1</sup> Case No. 2005-00433, The Joint Application of Nuon Global Solutions USA, BV, Nuon Global Solutions USA, Inc., AIG Highstar Capital II, LP, Hydro Star, LLC, Utilities, Inc. and Water Service Corporation of Kentucky for Approval of an Indirect Change in Control of A Certain Kentucky Utility Pursuant to the Provisions of KRS 278.020(5) and (6) and 807 KAR 5:001, Section 8, Response to Item3 of Commission Staff’s First Data Request.

26. Refer Water Service's response to Commission Staff's First Data Request, Item 3 at 14, "Pro Forma Plant to be Included in Rate Case." The total cost for the project to replace the 100 year old clear well tank is \$419,622. Explain why Water Service did not request a Certificate of Public Convenience and Necessity before it began construction of this project.

27. In its Order in Case No. 10481,<sup>2</sup> the Commission stated that "[a]djustments for post test-period additions to plant in service should not be requested unless all revenues, expenses, rate base, and capital items have been updated to the same period as the plant additions."

a. State whether Water Service's application is in complies with this requirement.

b. Identify each adjustment that Water Service proposes to its revenues, expenses, rate base, and capital that follow this post test-period requirement.

28. Administrative Regulation 807 KAR 5:001, Section 10(1), provides that all applications for a general rate adjustment shall be supported by either a "twelve (12) month historical test period which may include adjustments for known and measurable changes" or a "fully forecasted test period." Given that Water Service had the option to file a forecasted test period, explain why adjustments to reflect estimated post test-period plant additions and inflationary expense adjustments should be allowed in a rate case with an historical test-period.

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<sup>2</sup> Case No. 10481, Notice of Adjustment of the Rates of Kentucky-American Water Company Effective on February2, 1989 (Ky PSC August 22, 1989) at 5.

29. Refer to the Distribution of Expenses Year End 2004. Throughout this document there are numerous references to distribution codes. List and describe each code, explain how it is calculated.

30. Refer to the Distribution of Expenses Year End 2004 SE 50, Distribution of Direct Salaries and Benefits Year Ended 12/31/04 at 8. Provide an explanation and description of the services that were provided to support the direct allocation of the \$10,036 operator's salary from Northern Carolina to Water Service. Is this a normal occurrence and identify the amount that is included in the pro forma operations.

31. Refer to the Distribution of Expenses Year End 2004 SE 60, Distribution of General Expenses.

a. This document consists of 341 pages, but only pages 34 through 42 were provided. Describe the information that is contained on the missing pages and explain why these pages were not provided.

b. Provide a breakdown of salaries-office \$1,594,956 and describe the services that these employees provide Water Service.

c. Provide a breakdown of the bank service charges of \$227,072.

32. Refer to the Distribution of Expenses Year End 2004 WSC Rate Base.

a. State whether Water Service's requested rate base includes the allocation of the Service Company's rate base. If yes, state where this allocation is recorded and the amount.

b. Identify the proceedings in which this Commission has allowed a utility to recover the allocation of the Service Company's rate base.

33. Refer to the Annual Report of Utilities of Kentucky, Inc. to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 1998 at 23 "Statement of Retained Earnings."

a. Provide a detailed explanation of the acquisition adjustment debit that reduces retained earnings by \$1,702,742.

b. State the effect to Water Service's rate base, capital structure, and revenue requirement if this adjustment were reversed.

34. In response to Question 18 of her direct testimony, Ms. Weeks explains that Water Service is proposing that its rates be determined by utilizing the rate of return on rate base methodology. Given that the requested rate base exceeds Water Service's capital structure by \$837,426,<sup>3</sup> explain why the stockholders are entitled to earn a return in excess of the amount they actually have invested.

35. Refer to Water Services response to Commission Staff's First Data Request, Item 20. List each fringe benefit offered to Water Service Corporation employees and state the cost to be allocated to Water Service of each benefit by employee for 2004, 2005 and the expected cost in 2006.

36. Refer to Water Services response to Commission Staff's First Data Request, Item 22. Explain how Water Service developed the budget for salaries and wages if there is no budgeted number of employees.

37. Refer to Water Services response to Commission Staff's First Data Request, Item 25. Provide the group medical insurance policy for Water Service Corporation.

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<sup>3</sup> \$5,205,581 (Application, Exhibit 10, Rate Base) - \$4,368,155 (November 3, 2005 filing, Total Capitalization) = \$837,426.

38. Refer to Water Services response to Commission Staff's First Data Request, Item 29. Explain why the contract is not currently available. Provide copies of the contract when it is available.

39. Explain how the proposed rates were calculated. Show all calculations and state all assumptions used to develop the rates.

40. If a cost of service study was completed, provide a paper copy as well as a electronic copy in Excel or Lotus 1-2-3 format. If these formats are unavailable, provide data in rich text format (RTF).

41. Refer to the prepared testimony of Kirsten Weeks at question 9.

a. State whether any expenses are specific to a geographical area.

b. State whether the company has maintained separate financial records for each location so that a separate rate structure could be developed for each location.

c. If the response to 41(b) is yes, provide all detailed records related to each location and show all calculations, state all assumptions and provide workpapers associated with these records.

42. Refer to Water Services response to Commission Staff's First Data Request, Item 1. Identify the electronic format in which usage information is provided. State the electronic formats to which this information be converted to.

43. At paragraph 5 of its Application, Water Service states that the proposed rates are to recover, among other things, debt service, but latter indicates in its Application there is no debt related to its operations in Kentucky. Reconcile these statements



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Beth O'Donnell  
Executive Director  
Public Service Commission  
P. O. Box 615  
Frankfort, KY 40602

Dated: 1/17/06

cc: Parties of Record

Water Service Corporation of Kentucky  
Case No. 2005-00325

Employee Schedule

Employee Reference	Title	Date of Hire	Length of Employment	Wage Rate Effective 01/01/05	Wage Rate Implemented 10/15/05	Test-Period Regular Hours
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