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September 30, 2005

Beth O'Donnell
Executive Director
Public Service Commission
211 Sower Blvd.
Frankfort, KY 40601

Re: Case No. 2005-00348

Dear Ms. O'Donnell:

Please file the attached responses to the Commission's and Attorney General's data requests. Item 39 of the Commission's questions asks for an electronic copy of certain information. Due to technical problems with transmitting this information, it is not available to file today. It will be filed as soon as the person responsible for its preparation returns to his office next week.

Submitted by:
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PUBLIC SERVICE COMMISSION

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

The Joint Application of Kentucky Frontier Gas, LLC	)	
Belfry Gas, Inc., Floyd County Gas (East Kentucky Utilities, Inc.)	)	
Elam Utility Company, Inc., and Mike Little Gas Company for	)	Case No.
approval of transfer and acquisition of assets and stock, issuance	)	2005-00348
and assumption of debt, and issuance of a certificate	)	
of convenience and necessity, if necessary.	)	

RESPONSES TO STAFF DATA REQUEST NO. 1

Kentucky Frontier Gas, LLC ("KFG" or "Frontier"), Belfry Gas, Inc., Floyd County Gas, formerly East Kentucky Utilities, Inc., Elam Utility Company, Inc. and Mike Little Gas Company, by counsel, respond to the Commission Staff's Interrogatories and Requests for Documents filed September 16.

Responses are numbered identically to Staff's questions, with a brief recap of the issue. References are made to the "Transfer Application" which initiated the above-stated case to consolidate four existing utilities; the "Finance Application" made separately to request new debt and equity financing related to these utilities; and the "GOLD Application" to the Kentucky Governors Office for Local Development for reconfiguration of the existing utilities' state-administered low-interest loans.

The witness for all responses is Steve Oxford.

1. At page 3 of the Joint Application, the Joint Applicants state that "[p]urchase prices are based on the industry standard of $1000 per meter." Identify the source of this industry standard.

1. "Industry standard of $1000 per meter". There is no known compiled source for this number. Steven Shute first heard it in the 1980's while working at KN Energy, now part of Kinder-Morgan, a large Plains-based utility which consolidated many smaller companies. Since then, many subsequent utility sales have been closely scattered around that figure. It applies to large and small transactions for utilities with mature rate bases.

2. List the assets of Floyd County Gas that Kentucky Frontier acquired as a result of its winning public bid.

2. "Assets of Floyd County Gas" are listed in Exhibit 2 of the Transfer Application. No other information is currently available.

3. Explain the statement set forth at page 3 of the Joint Application that "[t]he purchase of assets did not include EKU [East Kentucky Utilities]."

3. EKU was a non-profit entity formed to operate the Floyd County gas system. In April 2005, Floyd County placed the utility assets up for public bid, but did not offer ownership in EKU. Applicant KFG has no knowledge of EKU's structure or ownership.

4. At page 3 of the Joint Application, the Joint Applicants state that "[t]he owner of Belfry Gas will transfer the assets of the distribution entity, including the CPCN [certificate of public convenience and necessity], but will retain some of the transmission pipelines and the Belfry name."

a. State whether the Annual Report that Belfry Gas filed with the Commission for the calendar year ending December 31, 2004, includes the transmission pipelines that will be retained.

b. If yes, provide the original cost and accumulated depreciation on the transmission lines.

4. The Belfry Annual Report does not include transmission lines.

Belfry considers all of its lines to be gathering or distribution. Any lines retained by Belfry will be considered gathering.

5. At page 4 of the Joint Application, the Joint Applicants state that "no acquisition adjustment is being requested at this time." Describe how, given that the purchase price for the assets exceeds the assets' net book value, the purchase can be recorded for accounting purposes without recording a plant acquisition adjustment.

5. This statement was intended to mean that KFG would not initially request a rate change due to increased acquisition values of assets. The purchase will be recorded for accounting purposes with the values paid for assets acquired.

6. State why customers of Elam Utility Company, Inc. ("Elam") and Mike Little Gas Company ("Mike Little") will continue to be served under Elam's and Mike Little's names rather than under the name of "Frontier Gas."

6. KFG will purchase the stock of these companies, along with the Certificates and other filed PSC rights. The other entities EKU and Belfry are not available to KFG. The corporate name of EKU was not purchased by Frontier. See Response 2. Belfry will retain its name, but transfer certain assets to Frontier. Because those operating names are not part of the acquisition, Frontier cannot provide service using those names.

As stated in 11.e, KFG plans to keep the existing rates "for at least 18-24 months, then to file a consolidated rate case to combine all utilities into a common rate". KFG is ambivalent about which brand or brands to use for the initial 2 years, and will follow Commission's directive on that issue. KFG cannot immediately fold all utilities into a single brand with a consolidated General Rate case, because such a requirement will delay the acquisition process past the winter of 2005-06, and a consolidated Test Year is unknowable without a year or two of consolidated operations. For all these reasons, Frontier intends to continue with the Elam and Mike Little brands and rates, while converting the Belfry and Floyd County customers to the Frontier brand but at the existing respective rates.

7. For each utility that Kentucky Frontier is acquiring, list all balance sheet items as reported in that utility's Annual Report to the Kentucky Public Service Commission for the Calendar Year Ending December 31, 2004 that Kentucky Frontier will acquire. State these balances as of December 31, 2004 and as of the date on which the Joint Applicants filed their application

7. The balance sheets for end of 2004 are available as Annual Reports on the PSC website. Frontier has not other information to supplement or revise that information. KFG is acquiring "plant" assets only. None of the utilities to be acquired routinely generates a monthly balance sheet. After acquisition, that information will be available for KFG tp prepare balance sheets and can be supplied to the Commission.

8. State Gilmer Mickey's qualifications to serve as Kentucky Frontier's chief financial officer.

8. Mr. Mickey has been the sole financial officer for Pinedale Natural Gas since its founding in 1993. PNG is a certificated utility in Wyoming with about 850 customers.

9. State where the day-to-day accounting and billing and collection functions for each acquired utility will occur after the proposed transfer occurs.

9. "Day-to-day accounting and billing and collections" along with payroll and accounts payable are planned to be consolidated for all utilities at the Prestonsburg-area office. Deposits and customer reconciliation will be done locally. Higher-level accounting such as financial statements and gas balancing will be handled by the Denver-area partners.

10. State the number of offices Kentucky Frontier will maintain when the transfer takes place and the estimated cost to maintain those offices.

10. "Number of offices" is presently planned to be a single business office in the Prestonsburg area. All O&M costs attributable to office expenses are at that office. Over the first years of operations, Frontier will evaluate the need for additional small field yards or facilities in each operating area.

11. Each of the utilities that Kentucky Frontier proposes to acquire have filed annual reports with the Commission for the calendar year ending December 31, 2004, that show a customer deposit liability. State whether this liability will transfer to Kentucky Frontier. If no, state whether these deposits will be refunded to customers prior to the proposed transfer.

11. "Customer deposit liability" will transfer to KFG.

12. Commission regulations require that interest be paid on customer deposits annually. Belfry's Annual Report to the Kentucky Public Service Commission for the Calendar Year Ending December 31, 2004 indicates that it owes interest to its customers on deposits of $19,483. Identify the entity that will be responsible for this liability and state when it will be paid to customers.

12. "Customer deposit interest" liability will transfer to KFG. Repayment will be evaluated after completion of the transfer when verification of deposits and customer records can be made.

13. Monthly filings of Elam in Case No. 2003-00171 indicate that the utility owes interest on customer deposits of $4,045 as of June 30, 2005. Identify the party or parties who will be responsible for this liability and state when this liability will be paid.

13. "Elam deposits" liability will transfer to KFG. Repayment will be evaluated after completion of the transfer when verification of deposits and customer records can be made.

14. At page 13 of the Application, the Joint Applicants state that the acquisition cost of the Belfry system is $750,000. In his letter of January 19, 2005 to J.W. Kinzer, Steven Shute states a purchase price of $700,000. State the purchase price that Kentucky Frontier will pay for Belfry stock.

14. At page 13 of the Application, the Joint Applicants state that the purchase price includes farm tap customers controlled by Mr. Kinzer but not currently in the Belfry system.

a. State the number and identify the location of these farm tap customers.
b. Identify the lines and source of supply for these customers.

14. [Note: Staff request has two question 14s.] "Belfry acquisition cost" is $750,000. The original Agreement for Sale was an offer to purchase of $700,000. After inspecting the distribution system it was determined that several miles of steel pipe were still in service and would likely have to be replaced with PE at an estimated cost of $200,000. In discussion and negotiations with Mr. Kinzer, parties decided that KFG could purchase at least 300 farm tap meters at a value of $250,000. The net acquisition price is $750,000.

14.

a. "Kinzer farm taps" There are about 190 taps on Kinzer's gathering systems and about 310 taps on Alert's gathering system located along Old Highway 23 west of Pikeville. Frontier expects to purchase at least 300 of these taps.

b. "Source of supply for farm taps" All the subject farm taps are situated on gathering and transmission pipelines operated by entities controlled by Kinzer. The gas supply for the farm taps will come from wells located on the gathering systems in accordance with various lease agreements. A secondary source could be the intrastate or interstate gas lines to which the gathering systems are connected.

15. In his letter of June 23, 2005 to Wilma Ison, Robert J. Oxford on behalf of Interstate Gas Services ("IGS") offers to purchase Elam's stock for $750,000, even though IGS has determined "the fair market value of the Company to be about $720,000.

a. Explain why an offer in excess of Elam's fair market value was made.
b. Provide all calculations of the incentive to Elam based on sales in excess of a base volume.

15. a. "Fair market value of Elam" was determined by IGS to be $720,000 as the most accurate of several valuation methods. The owner of Elam insisted on a much higher value, and the parties compromised on $750,000. There is no easy way to determine FMV of a small utility, especially one which is losing money. KFG believes that Elam has upside potential with several prospective customers which justifies paying slightly more than one of its FMV models.

b. "Calculations of the incentive to Elam". Ongoing employment was one of the key negotiating points for the owner of Elam. KFG agreed to a 5-year employment contract at a base salary. KFG also agreed in principle to an incentive program which would reward Ms. Ison for successfully recruiting customers that would add new load to the utility. These speculative customers are not included in the Application proforma. Exhibit A to the purchase contract has not been finalized. As envisioned by KFG, the formula would be as follows:

Incentive = x% of (Ave Annual dQ)(Rate)

Where x is a sliding amount depending on dQ

dQ is the additional MCF gas load

Rate is the General Rate for 2 or more MCF (now $4.30)

16. Refer to letter of January 19, 2005 from Steven Shute to J.W. Kinzer regarding "Agreement for Sale of Belfry Gas, Inc." Provide all exhibits to this letter including those attached after the letter's execution.

16. "Exhibits to Kinzer letter" of January 19, 2005. There were no exhibits to this letter.

17. Refer to letter of June 23, 2005 from Robert J. Oxford to Wilma Ison regarding "Agreement for Sale (Revised) Elam Utility Company, Inc." Provide all exhibits to this letter including those attached after the letter's execution.

17. There were no exhibits to this letter.

18. Refer to letter of January 14, 2005 from Robert J. Oxford to Miki Thompson regarding “Agreement for Sale Mike Little Gas Company, Inc.” Provide all exhibits to this letter including those attached after the letter’s execution.

18. There were no exhibits to this letter.

19. State whether Kentucky Frontier's acquisition of Belfry is a stock purchase.

19. KFG is purchasing the assets of Belfry, not the stock. The assets consist of the gas distribution system and connections to Kinzer's gas gathering system and Columbia Gas' system. In addition, to compensate KFG for the expense of replacing steel pipe with plastic pipe, KFG will take title to at least 300 farm taps owned by Kinzer and Alert.

20. State whether the documents set forth in Exhibit 2 of the Joint Application are the only documents evidencing the proposed purchase. If no, provide all other documents executed by the parties that evidence the proposed purchases.

20. These are the only purchase agreement documents.

21. Refer to the Joint Application, Exhibit 2. Explain why the letters within this Exhibit provide that the proposed purchase amounts may change.

21. These letters were sent to owners before KFG could perform any due diligence. Any significant change to the publicly-reported information for customers, gas volumes, DOT safety inspections system assets, and other major topics could have significantly changed the price KFG was willing to pay for the system. In its investigations, KFG found no such glaring deficiencies. See No. 19 above concerning the adjustment for the expense of replacing Belfry's steel system with plastic pipe.

22. Refer to the Joint Application, Exhibit 2. Explain the absence of any mention of Kentucky Frontier in any of the documents within this Exhibit except for those discussing East Kentucky Utilities.

22. At the time the letter offers were first made, Kentucky Frontier Gas LLC had not yet been formed. Rather than use a yet non-existent corporate name, partners chose to make the offers in the name of IGS and on behalf of the other partners.

23. In his letter of June 23, 2005 to Wilma Ison, Robert J. Oxford states that the net purchase price is equal to the purchase price minus the reduced GOLD debt and minus the Phillips loan payoff. State the current balance of the Phillips loan.

23. This is a personal loan to Wilma Ison from the former owners of Elam Utilities. Ms. Ison is responsible for the payoff of this loan at closing. The balance due is about $125,000.

24. Refer to Joint Application, Exhibit 6 at 1. The Column labeled "2006" shows meter fee revenue of $75,000 for residential customers and $9,900 for commercial customers. Describe how these amounts were derived. Show all calculations and state all assumptions used.

24. Because of the widely-disparate rates charged by the 4 companies, the combined revenue is difficult to model. The "First MCF is X, then…" rate structure is also dated; KFG will move eventually toward a minimum monthly fee, then a flat MCF rate. See the "Present Rates" sheet at the "Proforma Model" line. Using each utility's number of meters and rates, the weighted average rates come out to about

$2.50 per month minimum charge, plus

$4.50 per MCF rate for all MCF

The proforma model reflects these averages. For Residential and Commercial customers, this figure is calculated as:

No. of Meters x $2.50 per month x 12 months