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Department of Public Protection

Honorable John N. Hughes
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124 West Todd Street
Frankfort, KY 40601

October 30, 2006

RE: Case No. 2006-00398

We enclose one attested copy of the Commission's Order in the above case.

Sincerely,

A handwritten signature in black ink, appearing to read "Beth O'Donnell".

Beth O'Donnell
Executive Director

BOD/jc
Enclosure



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Office of the Attorney General Utility & Rate Intervention Division
1024 Capital Center Drive
Suite 200
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COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF NORTHERN KENTUCKY)	
WATER DISTRICT FOR APPROVAL OF)	CASE NO. 2006-00398
DEPRECIATION STUDY)	

O R D E R

On August 31, 2006, Northern Kentucky Water District ("NKWD") applied to the Commission for approval of its Depreciation Report. Having reviewed the proposed Depreciation Report and finding that further proceedings are necessary to determine its reasonableness, IT IS HEREBY ORDERED that:

1. The procedural schedule set forth in Appendix A shall be followed.
2. a. All responses to requests for information shall be appropriately indexed. Each copy of the data requested should be placed in a bound volume with each item tabbed. All responses shall include the name of the witness who will be responsible for responding to the questions related to the information provided, with copies to all parties of record and 8 copies to the Commission.
 - b. Each response shall be under oath or 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.
 - c. A party shall make timely amendment to any prior response if it obtains information upon the basis of which it knows that the response was incorrect when made, or though correct when made is now incorrect in any material respect.

d. For any request to which a party refuses to furnish the requested information that party shall provide a written explanation of the specific grounds for its failure to furnish.

3. At any hearing in this matter, neither opening statements nor summarization of direct testimony shall be permitted.

4. Motions for extensions of time with respect to the schedule herein shall be made in writing and will be granted only upon a showing of good cause.

5. All documents that this Order requires to be filed with the Commission shall be served upon all other parties.

6. Service of any document or pleading shall be made in accordance with 807 KAR 5:001, Section 3(7), and Kentucky Civil Rule 5.02.

7. NKWD shall give notice of the hearing in accordance with the provisions set out in 807 KAR 5:011, Section 8(5). At the time publication is requested, NKWD shall forward a duplicate of the notice and request to the Commission.

8. NKWD shall, no later than November 8, 2006, file with the Commission the information requested in Appendix B, with a copy to all parties of record. NKWD's response shall conform to the requirements set forth in Paragraph 2 of this Order.

9. Nothing contained herein shall prevent the Commission from entering further Orders in this matter.

Done at Frankfort, Kentucky, this 30th day of October, 2006.

By the Commission

ATTEST

Executive Director

Case No. 2006-00398

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 2006-00398 DATED OCTOBER 30, 2006.

NKWD shall file with the Commission and serve upon all parties of record its responses to the information requested in Appendix B no later than 11/13/06

All parties and Commission Staff shall serve their requests for information to NKWD no later than 12/01/06

NKWD shall file with the Commission and serve upon all parties of record its responses to the requests for information no later than 12/15/06

All parties and Commission Staff shall serve their supplemental requests for information upon NKWD no later than 01/02/07

NKWD shall file with the Commission and serve upon all parties of record its responses to the supplemental requests for information no later than 01/19/07

Intervenor testimony, if any, shall be filed with the Commission in verified prepared form no later than 02/05/07

All requests for information to any Intervenor shall be served upon that Intervenor no later than 02/19/07

Intervenors shall file with the Commission and serve upon all parties of record their responses to the requests for information no later than 03/05/07

NKWD may file with the Commission the testimony of its rebuttal witnesses in written verified form no later than 03/19/07

Last day for NKWD to publish notice of the hearing date..... (To be scheduled)

Public Hearing is to begin at 9:00 a.m., Eastern Standard Time, in Hearing Room 1 of the Commission's offices at 211 Sower Boulevard, Frankfort, Kentucky, for the purpose of cross-examination of witnesses of NKWD and Intervenors (To be scheduled)

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2006-00398 DATED OCTOBER 30, 2006.

FIRST DATA REQUEST OF COMMISSION STAFF TO NORTHERN KENTUCKY WATER DISTRICT

1. In selecting Black & Veatch Corporation ("Black & Veatch") to perform NKWD's Depreciation Report, did NKWD issue a request for proposal ("RFP")?

a. If NKWD issued an RFP, provide a copy of the RFP that was issued, identify the firms to which the RFP was sent, identify the firms that responded and explain why Black & Veatch was chosen.

b. If NKWD did not issue an RFP, explain how NKWD choose Black & Veatch to perform the Depreciation Report.

2. a. Provide the total cost to NKWD of the Black & Veatch Report on Depreciation Accrual Rates Water Utility Property of Northern Kentucky Water District August 2006 ("Depreciation Report").

b. Provide the minutes of the Board of Commissioners meeting in which Black & Veatch was approved to perform the depreciation survey.

3. Provide all correspondence, analyses, notes, memoranda, studies, minutes of meetings, and related documents that were prepared by either NKWD or Black & Veatch regarding the Asset Management Program.

4. Provide all correspondence, analyses, notes, memoranda, studies, minutes of meetings, and related documents that were prepared by either NKWD or Black & Veatch regarding the Asset Depreciation Report.

5. In its August 30, 2006 cover letter to the Depreciation Report, Black & Veatch states that, “[b]ased on our studies, in order to better assure recovery of plant investment over the useful life of plant in service, we recommend implementation of the rates set forth in Section 6 of this report.” Describe the studies referenced by Black & Veatch and provide copies.

6. At page 4 of the Depreciation Report, Black & Veatch states that, “[D]uring the course of our studies, we have not made an analysis, verified, or rendered an independent judgment as to validity of the information provided by others, including NKWD.”

a. Given this statement, explain how the Commission is able to rely upon the survey results and to render a decision on the reasonableness of Black & Veatch’s depreciation recommendations.

b. Explain why Black & Veatch did not determine the validity of the information it was reviewing.

7. At page 4 of the Depreciation Report, Black & Veatch states that, “[T]he methodologies we utilize follow generally accepted practices and reflects our experience and judgment, industry practice, and NKWD historical experience.”

a. List and describe the generally accepted depreciation practices that Black & Veatch followed in developing its proposed depreciation methodology.

b. Describe the industry practice that Black & Veatch followed in developing its proposed depreciation methodology.

c. Describe Black & Veatch’s experience and judgment that was used in developing the proposed depreciation methodology.

d. At page 6 of his direct testimony, Larry W. Loos states that, “[N]KWD does not maintain a CPR,¹ there is no comprehensive record of historical additions and retirements.” Given this statement, list and describe in detail the historical experience Black & Veatch relied upon to develop its proposed depreciation methodology. Explain how NKWD’s historical experience impacted the methodology Black & Veatch used.

8. At page 4 of the Depreciation Report, Black & Veatch states that it has “[m]ade assumptions with respect to conditions, events, and circumstances that will occur in the future.”

a. List and describe the future assumptions that were made by Black & Veatch. Explain the effect these assumptions have on the recommended depreciation rates.

b. Describe the effect to the proposed depreciation rates, if the future conditions, events, and circumstances do not occur as Black & Veatch assumed.

9. Provide a copy of the two most recent depreciation studies performed by Mr. Loos using each of the following techniques. In total there should be 6 studies provided in response to this request. Provide the Commission’s orders addressing and/or approving each of the studies provided.

- a. Survivor curve analyses.
- b. Simulated plant balance approach.
- c. Benchmarking of depreciation rates for other regional utilities.

¹ Continuing Property Record.

10. Provide a copy of the two most recent depreciation studies performed by Black & Veatch other than those performed by Mr. Loos using each of the following techniques. In total there should be 6 studies provided in response to this request. Provide the Commission orders addressing and/or approving each of the studies provided.

- a. Survivor curve analyses.
- b. Simulated plant balance approach.
- c. Benchmarking of depreciation rates for other regional utilities.

11. At page 3 of his direct testimony, Mr. Loos lists the state regulatory bodies where he has provided expert witness testimony.

a. Identify those state regulatory bodies where Mr. Loos presented a Depreciation Report and provided testimony.

b. For those jurisdictions identified in 11(a), provide copies of the Depreciation Report, of Mr. Loos Direct Testimony, and the regulatory final decision regarding the proposed Depreciation Report.

12. List all payments made to Black & Veatch over the previous 10 calendar years and the current year up to the date of the response to this request. For each payment provide the date of payment, check number, and description of the project for which each payment was made. Separate the payment amount by project where a single payment was made for multiple projects. From this response the amounts paid to Black & Veatch for the preparation of rate cases, asset management plan, Depreciation Report, and any other services for any given year should be apparent.

13. List anticipated payments in the next 12 months to Black & Veatch and identify the project for which the payments will be made.

14. List all NKWD Accounting Staff. On this list indicate which employees are responsible for property, plant and equipment accounting and state each employee's responsibilities in that regard.

15. Do the employees listed in response to Item 14 have the capability to account for property, plant and equipment in accordance with the accounting instructions and plant matrix set out in the Uniform Systems of Accounts for Class A and B Water Districts and Associations ("USoA")?

16. a. Does NKWD have the capabilities within its property, plant and equipment accounting system to record new plant purchases and installation projects to the water utility plant accounts stated in the USoA and individually state for each purchase or installation project the date placed into service, a project description or name, depreciable life, current charge to depreciation and accumulated reserve to date?

b. If the response to 16(a) is yes, provide such a plant schedule for all plant placed into service beginning January 1, 2005 through the date of this request.

c. If the response to 16(a) is no, explain why.

17. Provide a copy of the "Tax Asset Detail" as referenced in the Depreciation Report at page 8 in the most complete detailed form available to NKWD.

18. At page 17 of the Depreciation Report, reference is made to "NKWD's aggressive rehabilitation and replacement program" with regard to transmission and distribution mains.

a. List for each of the previous 10 years expenditures made for this program separating all expenditures annually by project name and number.

b. Provide the anticipated or budgeted amounts to be paid over the next 10 year period (or longer term if NKWD has forecasted further than 10 years) for this program separating all anticipated expenditures annually by project name and number.

c. The response to this request shall separate and identify the amounts paid for this program by the amounts capitalized as an asset and the amounts charged to operating expenses.

19. The Depreciation Report restates depreciation expense for an annual period ending December 31, 2004. At page 8 of his testimony, Mr. Loos states that the District intends to use depreciation rates approved by the Commission in this case for the purposes of determining annual depreciation rates going forward. Clarify the rates and method intended to be used by the District on a going forward basis. Is it NKWD's intention to apply the remaining lives as determined in the Depreciation Report to plant placed into service subsequent to December 31, 2004 or is it the District's intention to apply "whole life" depreciable lives to this plant as determined reasonable by the Depreciation Report?

20. Describe the process used to determine the survey population.

21. List all utilities surveyed that are not included in table 3-1 of the Depreciation Report.

22. a. State whether NKWD agrees or disagrees with this statement: The remaining lives used in the Depreciation Report were derived from the whole life depreciation rates of the surveyed regional utilities.

b. Provide all evidence showing that the lives presented by the surveyed utilities and relied upon to form the basis of the Depreciation Report do in fact represent whole life depreciation rates and not remaining lives.

c. Describe the effect on Black & Veatch's depreciation report if some of the water utilities included in the survey use remaining life depreciation.

23. Provide all evidence showing that the surveyed utility's assets as listed in the Depreciation Report by NARUC plant account number are like or similar to those assets as recorded by NKWD in the same NARUC plant accounts.

24. Provide all depreciation studies of the surveyed utilities that were reviewed and analyzed by Black & Veatch as a part of its preparation of the NKWD Depreciation Report.

25. At page 11 of the Depreciation Report, Black & Veatch states that, "[W]e surveyed depreciation expense rates reported by 17 regional water utilities using data from annual reports, contacting utility representatives, and contacting commission staffs."

a. Describe the criteria Black & Veatch used in choosing the 17 regional utilities that it surveyed and that are listed in Table 3-1.

b. Did Black & Veatch consider using any other water utilities in its survey other than the 17 that were identified? If yes, list those utilities and provide an explanation as to why Black & Veatch did not include those utilities in its survey.

c. For each utility state if Black & Veatch used annual report data in the survey, the identify the year of the annual report, explain how the annual report was obtained, and provide the data Black & Veatch relied upon from the annual report.

d. For each utility state if Black & Veatch contacted a utility representative, identify the utility representative(s) Black & Veatch contacted, and provide the data Black & Veatch obtained.

b. For each utility state if Black & Veatch contacted a representative of a regulatory agency, identify the agency contacted, identify the Staff representative(s) that provided any information used in the survey, and provide the data Black & Veatch obtained.

26. Explain if NKWD agrees or disagrees with the statement that, a utility's maintenance program has an impact on the anticipated useful lives of a utility's assets.

27. Explain if NKWD agrees or disagrees that, generally, smaller utilities have less resources to dedicate toward maintenance programs than do larger utilities.

28. Table 3-1 of the Depreciation Report shows that the regional water utilities surveyed have customer bases ranging from 2,197 to 449,519. Why is it appropriate to base NKWD's depreciable lives on utilities that are significantly larger and smaller than NKWD?

29. a. Identify each utility listed in Table 3-1 that uses remaining life depreciation.

b. If some of the water utilities that were surveyed use remaining life depreciation, describe the impact this would have on Black & Veatch's depreciation report.

30. Provide all evidence of the surveyed utilities' maintenance programs reviewed by Black & Veatch in developing the Depreciation Report.

31. Refer to Appendix B of the Depreciation Report. Provide all evidence gathered, used and relied upon to determine the "forecast interim activity" and "final retirements" for each annual period.

32. Refer to page 22 of the Depreciation Report, Table 6-1, Recommended Depreciation Rates.

a. Provide all workpapers and supporting calculations for the "Existing Weighted Age" of each NARUC plant account.

b. Provide a revised Table 6-1 eliminating the redistribution of the accumulated depreciation reserve.

c. Explain in detail the impact the accumulated reserve redistribution has on the NKWD's future depreciation expense.

d. At page 3 of the Depreciation Report, Black & Veatch states that, "[W]e propose to redistribute these deficiencies to other accounts so that the resulting reserve ratio is more reasonable." Other than achieving a more reasonable reserve ratio, explain in detail what is achieved by the proposed redistribution of NKWD's accumulated reserve deficiencies.

e. Explain the significance and implications to NKWD if the Commission denied the redistribution of "reserve deficiencies" as proposed in the Depreciation Report.

f. Would the response to Item 32(e) change if the Commission finds as reasonable an overall composite depreciation rate of 3.0317² to be applied to all gross plant placed into service as of December 31, 2004 until fully depreciated and the Commission ordered the application of whole life depreciable lives to all plant placed into service subsequent to December 31, 2004.

g. Explain if NKWD agrees to the method of calculating depreciation expense described in Item 32(f) where remaining life depreciation is applied to pre-2004 utility plant in service, but whole life, straight line depreciation is taken on post-2004 utility plant in service.

33. Provide the last two depreciation studies performed by Black & Veatch where the redistribution of "depreciation reserve" was approved by a Commission order. Also, provide the Commission orders addressing and/or approving the "depreciation reserve" redistribution.

34. At page 4 of the Depreciation Report, Black & Veatch recommend that NKWD "[a]gain review the adequacy of its depreciation rates in 4 to 5 years."

a. Provide a complete description of the depreciation review that Black & Veatch is proposing.

b. State who will perform this review.

c. State weather the review can be performed in-house by NKWD staff.

² Depreciation Expense 12/31/04	\$ 5,128,169
Add: NKWD's Proposed Adjustment	+ 2,190,986
Pro Forma Depreciation Expense	\$ 7,319,155
Divided by: Plant in Service 12/31/04	÷ 241,419,275
Composite Rate	<u>3.0317%</u>