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August 9, 2004

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AUG 09 2004

PUBLIC SERVICE
COMMISSION

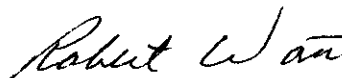
Hon. Elizabeth O'Donnell
Executive Director
Public Service Commission
211 Sower Boulevard
P.O. Box 615
Frankfort, KY 40601

Re: Delta Natural Gas Company, Inc.
Case No. 2004-00067

Dear Ms. O'Donnell:

We enclose for filing an original and 10 copies of the rebuttal testimony of Delta Natural Gas Company, Inc. in the above-captioned case. Thank you for your attention to this matter. Best regards.

Sincerely,



Robert M. Watt, III

Rmw

Cc: Counsel of Record (w/encl.)
Mr. John F. Hall (w/encl.)

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AUG 09 2004

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

PUBLIC SERVICE
COMMISSION

In the Matter of:

AN ADJUSTMENT
OF RATES OF DELTA NATURAL
GAS COMPANY, INC.

)
)
)

CASE NO. 2004-00067

REBUTTAL TESTIMONY OF

JOHN F. HALL

August 9, 2004

AFFIDAVIT

The affiant, John F. Hall, being duly sworn, deposes and states that the prepared testimony attached hereto and made a part hereof, constitutes the prepared rebuttal testimony of this affiant in Case No. 2004-00067, in the Matter of: An Adjustment of Rates of Delta Natural Gas Company, Inc. and that if asked the questions propounded therein, this affiant would make the answers set forth in the attached prepared rebuttal testimony.

Affiant further states that he will be present and available for cross-examination and for such additional examination as may be appropriate at the hearing in Case No. 2004-00067 scheduled by the Commission, at which time affiant will further reaffirm the attached prepared testimony as his rebuttal testimony in such case.

John F. Hall
John F. Hall

STATE OF KENTUCKY)
)
COUNTY OF CLARK)

Subscribed and sworn to before me by John F. Hall, this the 5th day of August, 2004.

My Commission Expires: 6/20/2008

Emily P. Bennett
Notary Public, State at Large, Kentucky

1 Q. Please state your name and business address.

2 A. John F. Hall, Delta Natural Gas Company, Inc., 3617 Lexington Road,
3 Winchester, Kentucky 40391.

4 Q. Have you previously filed direct testimony in this proceeding?

5 A. Yes.

6 Q. What is the purpose of this testimony?

7 A. My rebuttal testimony will discuss proposed changes in the treatment of three
8 items and will introduce a revised set of schedules and work papers, which
9 appeared at Tab 27 of the Filing Requirements in this case, as well as a revised
10 Income Statement, which appeared at Tab 42 of the Filing Requirements. The
11 revised schedules and income statement reflect the changes in the treatment of the
12 three items.

13 Q. Are you proposing a change in the treatment of employee bonuses?

14 A. Yes. In our original filings, the 2003 employee bonus was improperly reflected
15 because it did not reflect the allocation of the bonus to Delta's subsidiaries. The
16 item has been corrected, as discussed in response to PSC 3-12(b). It is reflected
17 in the revised schedules and work papers attached hereto. The employee bonus
18 change is reflected on Hall WP 4.1.

19 Q. Are you proposing a change in the treatment of customer deposits?

20 A. Yes. While we originally treated customer deposits the same way the
21 Commission did in Case No. 97-066, we understand that the Commission now
22 requires the exclusion of interest on customer deposits from operating expenses if

1 the customer deposit balance is not excluded from rate base. We, therefore, are
2 excluding interest on customer deposits from operating expenses.

3 Q. Is that change reflected on the attached schedules and work papers?

4 A. Yes. It appears on Schedule 4.

5 Q. Have you reflected the change in the Capital Structure discussed by John Brown
6 in his rebuttal testimony?

7 A. Yes. Schedule 9 reflects the change in the equity component of the capital
8 structure related to Minimum Pension Liability discussed by John Brown in his
9 rebuttal testimony.

10 Q. Does this conclude your rebuttal testimony at this time?

11 A. Yes.

Delta Natural Gas Co. Inc.
Cost of Service-Revenue Deficiency
Test Period Ended 12/31/03

Line Number				
1	Cost of Gas	Schedule 3	\$	33,364,884
2	O & M Expense	Schedule 4		10,375,862
3	Depreciation Expense	Schedule 5		4,045,073
4	Taxes Other Than Income	Schedule 6		1,509,727
5	Return	Schedule 7		9,573,187
6	Income Tax	Schedule 8		3,352,030
7	Total Cost of Service		\$	62,220,763
8	Revenues at Present Rates	Schedule 2		57,709,948
9	Revenue Deficiency		\$	4,510,815

Delta Natural Gas Co. Inc.
 O & M Adjustments
 Test Period Ended 12/31/03

Line Number			
1	Payroll Expenses	\$	120,697 Hall WP-4.1
2	Bonus		(317,865) Hall WP-4.1
3	Rate Case Expense-Amortize		
4	over 3 years		83,333 Hall WP-4.2
5	Customer Deposits		-
6	Adjust for lobbying expenses-		
7	other A/C's		(15,280) Hall WP-4.3
8	A/C 913 Advertising		(2,204)
9	A/C 930.1 Public and Community		
10	Relations		(25,645)
11	A/C Lobbying		(783)
12	A/C 930.04 Marketing		(15,239)
13	Total Adjustment	\$	<u>(172,986)</u>
14	Per Books		10,548,848
15	O & M as Adjusted		10,375,862

Delta Natural Gas Co. Inc.
Payroll Adjustment
Test Period Ended 12/31/03

Line Number		
1	Annualized Salaries and Wages	\$ 6,593,535
2	Pro Forma Capitalized Wages	
3	and Subsidiary Allocation	1,788,914

4	Pro Forma Salary and Wage	
5	Expense	4,804,621
6	Actual 2003 Test Year Salary	
7	and Wage Expense	4,683,924

8	Pro Forma Payroll Adjustment	120,697
9	Bonus Excluded	(317,865)

10	Total Payroll Adjustment	\$ (197,168)
		=====

Delta Natural Gas Co. Inc.
Payroll Tax Adjustment
Test Period Ended 12/31/03

Line Number

1	Direct Total Payroll for 12		
2	Months Ended 12/31/03	\$	6,559,613
3	Payroll Taxes (A/C 1.408.03)		496,228
4	Payroll Taxes Percent of Payroll		7.56%
5	Pro Forma Payroll Adjustment		120,697
6	Pro Forma Payroll Tax Increase		9,125
7	Bonus Taxes		(20,628)
8	Total Payroll Tax Adjustment	\$	(11,503)
9	Other Taxes per Books		1,521,230
10	Other Taxes as Adjusted	\$	1,509,727

Delta Natural Gas Co. Inc.
Rate Base
Test Period Ended 12/31/03

Line Number		
1	Plant in Service	\$ 165,994,418
2	Depreciation Reserve	(52,964,026)
3	Net Plant in Service	\$ 113,030,392
4	Cash Working Capital(1/8 of OM	1,296,983
5	Prepayments-13 ,mo av	351,876
6	Materials and Supplies-13 mo av	478,139
7	Gas in Storage-13 mo av	6,363,748
8	Accumulated Def Income Taxes	(14,697,866)
9	Unamortized Debt EXPENSE	4,185,070
10	Customer Deposits	-
11	Advances in Construction	(105,692)
12	Depreciation Adjustments	145,431
13	Unrecovered SFAS 143 Adopt Cost	30,133
14	Total Net Rate Base	\$ 111,078,214
15	Return @ 8.618 %	\$ 9,573,187

Delta Natural Gas Co. Inc.
Computation of Income Taxes
Test Period Ended 12/31/03

Line Number		
1	After Tax Return	\$ 9,573,187
2	Interest Deduction	4,263,207
3	Equity Portion of Return	----- 5,309,980
4	Tax Rate of 39.445%to Equity Return	2,094,522
5	ITC Amortization	(39,200)
6	Amortization of Excess Deferred Tax	(25,500)
7		----- \$ 2,029,822
8	Tax Expansion Factor	1.6513913
9	Total Income Tax Liability	----- \$ 3,352,030 =====

Delta Natural Gas Co. Inc.
 Income Tax Adjustment
 Test Period Ended 12/31/03

Line Number			
1	Operating Revenues	\$ 57,709,948	
2	Operating Expense w/o Income Tax	49,295,546	\$ 111,078,214 3.838%
3	Interest Expense	4,263,207	\$ 4,263,207
4	Taxable Income	\$ 4,151,195	
5	Combine State and Federal Tax Rate	39.445%	
6	Income Taxes	\$ 1,637,439	
7	ITC amortization	(39,200)	
8	Amortization of Excess Deferred Tax	(25,500)	
9	Adjusted Income Taxes	\$ 1,572,739	

Delta Natural Gas Company Inc
 Capital Structure
 Test Year End 12/31/2003

Line Number	Per Books Consolidated at 12/31/03	Elimate Subs	Adjusted Capital Structure	Ratios	Cost Rates	Weighted Cost of Capital
1 Equity	\$ 46,080,957	\$ (1,165,275)	\$ 44,915,682	38.24%	12.500%	4.780%
2 L/T Debt	54,824,000		54,824,000	46.68%	7.422%	3.464%
3 S/T Debt	17,707,889		17,707,889	15.08%	2.478%	0.374%
4 Total	<u>\$ 118,612,846</u>	<u>\$ (1,165,275)</u>	<u>\$ 117,447,571</u>	<u>100.00%</u>		<u>8.618%</u>

Line Number	Delta Natural Gas Company Inc		As Adjusted	Required Increase	Proposed	
	Test Year End	Income Statement				12/31/2003
	Per Books	Adjustments				
	12/31/2003					
1	Operating Revenue	\$ 52,085,352	\$ 5,264,596	\$ 57,709,948	\$ 4,510,814	\$ 62,220,762
2	Operating Expenses:					
3	Purchased Gas	\$ 27,846,732	\$ 5,518,152	\$ 33,364,884		\$ 33,364,884
4	O & M Expenses	10,548,848	(172,986)	10,375,862		10,375,862
5	Depreciation	4,190,504	(145,431)	4,045,073		4,045,073
6	Other Taxes	1,521,230	(11,503)	1,509,727		1,509,727
7	Income Taxes	1,291,201	281,538	1,572,739	1,779,291	3,352,030
8	Total Operating Expenses	\$ 45,398,515	\$ 5,469,770	\$ 50,868,285	\$ 1,779,291	\$ 52,647,575
9	Operating Income	\$ 6,686,837	\$ 154,826	\$ 6,841,663	\$ 2,731,524	\$ 9,573,187
10	Interest Expense	\$ 4,562,696	\$ (55,031)	\$ 4,507,665		\$ 4,507,665
11	Net Income	\$ 2,124,141	\$ 209,858	\$ 2,333,999	\$ 2,731,524	\$ 5,065,522
12	Return on Equity	4.73%		5.20%		11.28%