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COMMISSION



COMMONWEALTH OF KENTUCKY
OFFICE OF THE ATTORNEY GENERAL

GREGORY D. STUMBO
ATTORNEY GENERAL

1024 CAPITAL CENTER DRIVE
SUITE 200
FRANKFORT, KY 40601-8204

8 September 2005

Via Hand Delivery

Beth A. O'Donnell, Executive Director
Public Service Commission
211 Sower Boulevard
Frankfort, Kentucky 40601

RE: PSC Case No. 2005-00323

Dear Ms. O'Donnell:

As a consequence of discussions with Damon R. Talley, attorney for the Joint Applicants, and in light of information provided by the acquiring Joint Applicants during an informal conference, the Office of the Attorney will clarify and otherwise modify certain questions in its request for information. It will also withdraw certain other questions.

The Attorney General provides this notice to the Commission and asks that the Commission place this letter into the record for this case. A photocopy of the changes is attached.

Thank you for your consideration of this matter.

Sincerely,

David Edward Spenard

David Edward Spenard
Assistant Attorney General

cc: Damon R. Talley (e-mail)
Jerry Wuetcher (hand delivery)

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Attorney General's
Clarifications and Modifications to His
Request for Information

[Modification: Strike Additional Instruction]

~~Additional Instruction regarding AIG: While Hydro Star, LLC, is a Joint Applicant, Hydro Star's "parent companies" including American International Group, Inc. ("AIG") are not Joint Applicants. The Attorney General submits certain requests for AIG and asks that AIG provide the response.~~

1. [No change]
2. RE: Joint Application. With regard to AIG **Highstar Capital II**, please provide the following:
 - a. Please indicate whether AIG **Highstar Capital II's** holdings, as of 1 January 2005, include a controlling interest in any water or sewer utilities. If yes, provide the following:
 - (i) Provide a schedule identifying the utilities and the percentage of ownership;
 - (ii) Provide a schedule of jurisdictions for AIG **Highstar Capital II's** water operations; and
 - (iii) Provide a schedule of jurisdictions for AIG **Highstar Capital II's** sewer operations.
 - b. [No change]
 - c. [No change]
3. [No change]
4. RE: Joint Application. Will the purchase price of \$192,500,000.00 result in the creation of any goodwill ~~on the books of AIG or any of its subsidiaries or affiliates (hereinafter "AIG entities")~~? If yes, please provide the following:
 - a. Explain how ~~AIG or the AIG entities~~ **the acquiring Joint Applicants** will account for the goodwill created in the transaction.

- b. Explain how ~~AIG or the AIG entities~~ **the acquiring Joint Applicants** will amortize any goodwill created in the transaction.
 - c. Indicate whether ~~AIG and the AIG entities~~ **the acquiring Joint Applicants** will agree, as a condition of obtaining approval of this transaction, to forego recovery through Kentucky jurisdictional rates for any amount of goodwill that results from this transaction. If not, why not?
5. [No change]
6. Transaction Cost Information. [Modified Question] **Do the acquiring Joint Applicants intend to seek the creation of any regulatory asset as a result of this transaction? (For example, do the acquiring Joint Applicants intend to seek the creation of a regulatory asset for the cost-to-achieve the transaction?) If yes, provide a narrative of what the Joint Applicants seek including a discussion of any rate base treatment, amortization, and rate recovery for any regulatory asset resulting from this transaction.** [Withdraw remaining portions of original question]
7. RE: Costs relating to the transaction.
- a. Indicate whether ~~AIG and the AIG entities~~ **the acquiring Joint Applicants** will agree, as a condition of obtaining approval of this transaction, to forego recovery through Kentucky jurisdictional rates for any amount of costs-to-achieve the transaction. If not, why not?
 - b. Indicate whether ~~AIG and the AIG entities~~ **the acquiring Joint Applicants** will agree, as a condition of obtaining approval of this transaction, to forego recovery through Kentucky jurisdictional rates for any amount of post-transaction costs for blending. If not, why not?
8. ~~Has AIG~~ **Have the acquiring Joint Applicants** completed a due diligence review? If yes, indicate whether the review identifies any facts or circumstances that would have a material adverse effect on ~~AIG, any AIG entity,~~ the post-transaction Utilities, Inc., or the post-transaction Water Service and supply a summary of the review for the effect. If not, please provide an estimate of when the review will be complete and provide the response when available.

9. Please provide a full and complete copy of all media releases (including AIG website postings) by AIG regarding the proposed ~~merger~~ **transaction**.
10. [No change]
11. [No change]
12. [No change]
13. The following items represent conditions imposed by the Kentucky PSC in other proceedings pertaining to a utility acquisition or transfer of ownership or control. Consistent with Kentucky PSC precedent, as a condition to the approval of this Joint Application, will ~~AIG and the AIG entities~~ **the acquiring Joint Applicants** agree to the following?
- a. Will ~~AIG, and the AIG entities including Hydro Star, Utilities, Inc., and Water Service~~ **the acquiring Joint Applicants** commit to not declare and pay dividends out of capital or unearned surplus without prior approval of the Kentucky PSC?
 - b. Will ~~AIG, and the AIG entities including Hydro Star, Utilities, Inc., and Water Service~~ **the acquiring Joint Applicants** commit to maintain and house Water Service's books and records in Kentucky?
 - c. Will ~~AIG, and the AIG entities including Hydro Star, Utilities, Inc., and Water Service~~ **the acquiring Joint Applicants** commit that it will not assert in any judicial or administrative proceeding that the Kentucky PSC lacks for rate-making purposes jurisdiction over Water Service's capital structure, financing, and cost of capital?
 - d. Will ~~AIG, and the AIG entities including Hydro Star, Utilities, Inc., and Water Service~~ **the acquiring Joint Applicants** commit that it will obtain Kentucky PSC approval prior to the transfer of any Water Service asset with an original book value in excess of \$1 million or real property or real estate with a net original book value in excess of \$200,000?
 - e. Will ~~AIG, and the AIG entities including Hydro Star, Utilities, Inc., and Water Service~~ **the acquiring Joint Applicants** commit that neither Water Service nor its ratepayers, directly or indirectly, will incur any additional costs, liabilities, or obligations in conjunction

with ~~AIG's or Hydro Star's acquisition of Utilities, Inc.~~ **this transaction?**

- f. Will ~~AIG, and the AIG entities including Hydro Star, Utilities, Inc., and Water Service~~ **the acquiring Joint Applicants** commit to adequately fund and maintain Water Service's treatment, transmission, and distribution systems; comply with all applicable Kentucky statutes and administrative regulations; and supply the service needs of Water Service customers?
- g. Will ~~AIG, and the AIG entities including Hydro Star, Utilities, Inc., and Water Service~~ **the acquiring Joint Applicants** commit to obtaining Kentucky PSC approval prior to Water Service's payment of any dividend or transfers of any funds within a calendar year that collectively represent more than 5 percent of Water Service's retained earnings as of December 31 of the prior calendar year ~~to AIG or any AIG entity including Hydro Star and Utilities Inc.?~~
- h. Will ~~AIG, and the AIG entities including Hydro Star, Utilities, Inc., and Water Service~~ **the acquiring Joint Applicants** commit to notifying the Kentucky PSC in writing within 30 days of any downgrading of the bonds of AIG, Hydro Star, Utilities Inc., or any subsidiary of Hydro Star or Utilities Inc., and will include with such notice the complete report of the issuing bonding agency?
- i. Will ~~AIG, and the AIG entities including Hydro Star, Utilities, Inc., and Water Service~~ **the acquiring Joint Applicants** commit that Water Service will not incur any additional indebtedness, issue any additional securities, or pledge any assets to finance any part of the purchase price paid for Utilities Inc.'s stock?
- j. Will ~~AIG, and the AIG entities including Hydro Star, Utilities, Inc., and Water Service~~ **the acquiring Joint Applicants** commit that the payment for Utilities Inc.'s stock will not be recorded on Water Service's books?
- k. Will ~~AIG, and the AIG entities including Hydro Star, Utilities Inc., and Water Service~~ **the acquiring Joint Applicants** commit that any premium paid for Utilities Inc. stock, as well as all transaction-related costs including post-transaction costs for blending will not be "pushed down" to Water Service and will not be recovered from Water Service's ratepayers?

1. Will ~~AIG, and the AIG entities including Hydro Star, Utilities Inc., and Water Service~~ **the acquiring Joint Applicants** commit that the acquisition of Utilities Inc., will not affect the accounting and rate-making treatments of any of Water Service's excess deferred income taxes?

14. Do ~~AIG and the AIG entities~~ **the acquiring Joint Applicants** plan to create any additional corporations ~~that will be subsidiaries or otherwise new corporations within AIG~~ as part of this transaction? In answering this question, include any new corporations that ~~AIG and the AIG entities~~ **the acquiring Joint Applicants** currently plan to create within the twelve (12) month period following final approval of the transaction. If yes, identify the corporation(s) and provide a brief description of its function or purpose.

15. [No change]

16. ~~Do AIG and the AIG entities have~~ **Are there** any plans to terminate or alter any of Utilities Inc.'s or Water Service's existing affiliate agreements or contracts as part of this transaction? In answering this question, include any plans to terminate or alter affiliate agreements or contracts within the twelve (12) month period following final approval of the transaction. If yes, identify the agreement or contract and provide a summary of the change.

17. ~~Do AIG and the AIG entities anticipate~~ **Will** Utilities Inc., or Water Service ~~entering~~ into any new affiliate agreements or contracts as part of this transaction? In answering this question, include any plans for Utilities Inc. or Water Service to enter into new affiliate agreements or contracts within the twelve (12) month period following final approval of the transaction. If yes, identify the agreement or contract and provide a description of the function or purpose of each agreement or contract.

18. Will the merger result in any changes in accounting principles for either Utilities, Inc., or Water Service? ~~(For example, does AIG have the same accounting policy regarding the use of estimates, etc.?)~~ If yes, please summarize the change(s).

19. [No change]

20. [No change]

21. Utilities, Inc. is identified as the “direct parent” of Water Service Corporation of Kentucky (“Water Service”). With regard to this statement, please provide the following:

- a. Provide a diagram showing the present corporate structure that contains Water Service including all parents, subsidiaries, and affiliates.
- b. For each entity identified in sub-part a, provide a schedule that, by entity, shows the entity type (e.g. partnership, limited liability corporation), jurisdiction for the entity’s organization (e.g. state or country of incorporation), and percentage of ownership. Provide, for any applicable entity, the identity of any minority ownership interests in excess of 5%.
- c. Provide a diagram showing the ~~post-transaction corporate structure that contains Water Service including all parents within AIG as well as all subsidiaries and affiliates within the AIG Asset Management business segment~~ closing general ownership structure of Utilities, Inc., including the path from AIG Highstar Capital II to the AIG Global Investment Group and the latter’s Investment Committee.
- d. For each entity identified in sub-part c, provide a schedule that, by entity, shows the entity type (e.g. partnership, limited liability corporation), jurisdiction for the entity’s organization (e.g. state or country of incorporation **or organization**), and percentage of ownership. ~~Provide for any applicable entity, the identity of any minority ownership interests in excess of 5%.~~

22. [No change]

23. Withdrawn

24. Withdrawn

25. Withdrawn