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August 17, 2009

Jeff Derouen  
Executive Director  
Public Service Commission  
211 Sower Blvd.  
Frankfort, KY 40601

**RECEIVED**

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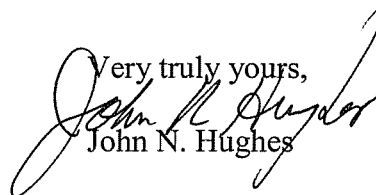
Re: Case No. 2008-00563

Dear Mr. Derouen:

Attached are corrected pages of Pauline Ahern's Pre-filed testimony. The debt/equity numbers were reversed in the rate of return calculation. This does not affect the requested return on equity or any other aspect of the application.

Also attached are the newspaper tear sheets and affidavits of publication for Clinton and Middlesboro providing notice of the hearing.

If you have any questions about this matter, please contact me.

Very truly yours,  
  
John N. Hughes

Attorney for WSCK

Attachments

Cc: Attorney General

1 A. The purpose is to provide testimony on behalf of Water Service Corporation of  
2 Kentucky WSCK), as to the appropriate overall rate of return which it should be  
3 afforded the opportunity to earn on its jurisdictional rate base.

4

5 **Q. What is your recommended range of overall rate of return?**

6 A. I recommend that the Kentucky Public Service Commission (KY PSC or the  
7 Commission) authorize the Company the opportunity to earn a range of common  
8 equity cost rate of 11.60%-12.10%, with a midpoint of 11.85% on the common  
9 equity financed portion of its jurisdictional rate base. A common equity range  
10 cost rate of 11.60%-12.10% results in a range of overall rate of return of 8.94% -  
11 9.17% (midpoint of 9.06%) based upon the consolidated capital structure at June  
12 30, 2008 of Utilities, Inc., the parent of WSCK, which consisted of 53.03% total  
13 debt and 46.97% common equity, at a debt cost rate of 6.58% and my  
14 recommended common equity cost rate range of 11.60%-12.10% as summarized  
15 on Table 1 below:

16

Table 1

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**Q. Have you prepared an exhibit which supports your recommended range of  
common equity cost rate?**

1 common equity cost rate is 11.60% - 12.10%, with a midpoint of 11.85%, and is  
2 applicable to the Company's requested common equity ratio of 46.97% at June  
3 30, 2008

4 .

5 **III. GENERAL PRINCIPLES**

6 **Q. What general principles have you considered in arriving at your**  
7 **recommended range of common equity cost rate of 11.60%-12.10%?**

8 A. In unregulated industries, the competition of the marketplace is the principal  
9 determinant of the price of a product or service. In the case of regulated public  
10 utilities, regulation must act as a substitute for such marketplace competition.  
11 Consequently, marketplace data must be relied upon to assure that the utility can  
12 fulfill its obligations to the public and provide adequate service at all times. This  
13 requires a level of earnings sufficient to maintain the integrity of presently  
14 invested capital and permit the attraction of needed new capital at a reasonable  
15 cost in competition with other firms of comparable risk, consistent with the fair  
16 rate of return standards established by the U.S. Supreme Court in the Hope and  
17 Bluefield cases cited previously. Consequently, in my determination of common  
18 equity cost rate, I have evaluated data gathered from the marketplace for utilities  
19 as similar in risk as possible to WSCK.

20

1 PMA- PMA-1. The average size premium for the decile in which each proxy  
2 group falls has been compared to the average size premium for the 10<sup>th</sup> decile in  
3 which WSCK would fall if its stock were traded and sold at the January 2, 2009  
4 average market/book ratio of 197.5% and 193.1% experienced by each proxy  
5 group, respectively. As shown on page 3 of Schedule PMA- 1, the size premium  
6 spread between WSCK and the seven AUS Utility Reports water companies is  
7 3.62% and between WSCK and the ten AUS Utility Reports natural gas  
8 distribution companies is 4.32%. Page 4 contains data in support of page 3 while  
9 pages 5 through 17 of Schedule PMA-1 contain relevant information from the  
10 Ibbotson SBBI – 2008 Valuation Yearbook discussed previously.

11 Consequently, a business risk adjustment of 3.62% is indicated based  
12 upon the seven AUS Utility Reports water companies and 4.32% is indicated  
13 based upon the ten AUS Utility Reports natural gas distribution companies.  
14 However, I will make conservatively reasonable business risk adjustments of  
15 0.35% (35 basis points) as shown on Line No. 6 on page 2 of Schedule PMA-1 to  
16 the indicated common equity cost rate range of 11.25% to 11.75%. This results  
17 in an indicated business risk adjusted common equity cost rate range of 11.60%  
18 to 12.10% (with a midpoint of 11.85%) as shown on Line No. 7, which is my  
19 recommended common equity cost rate range.

20 A common equity cost rate range of 11.60%-12.10%, when applied to  
21 the Company's requested common equity ratio of 46.97% estimated at June 30,  
22 2008 results in a range of overall rate of return of 8.94%-9.17% which, in my  
23 opinion, is both reasonable and conservative and will provide WSCK with

Water Service Corporation of Kentucky  
 Summary of Cost of Capital and Fair Rate of Return  
 Based on the Actual Consolidated Capital Structure of Utilities, Inc. at June 30, 2008

<u>Type of Capital</u>	<u>Ratios (1)</u>	<u>Cost Rate</u>			<u>Weighted Cost Rate</u>		
Debt	53.03%	6.58% (1)			3.49%		
Common Equity	46.97%	11.60% (2)	--	12.10% (2)	5.45%	--	5.68%
Total	<u>100.00%</u>				<u>8.94%</u>	--	<u>9.17%</u>

(1) Company provided.

(2) Based upon informed judgment from the entire study, the principal results of which are summarized on page 2 of this Schedule.

Water Service Corporation of Kentucky  
Market Capitalization of Water Service Corporation of Kentucky  
the Proxy Group of Seven AUS Utility Reports Water Companies,  
and the Proxy Group of Ten AUS Utility Reports Natural Gas Distribution Companies

Company	Exchange	1	2	3	4	5	6
		Common Stock Shares Outstanding at December 31, 2007 ( millions )	Book Value per Share at December 31, 2007 (1)	Total Common Equity at December 31, 2007 ( millions )	Closing Stock Market Price on January 2, 2009	Market-to-Book Ratio on January 2, 2009 (2)	Market Capitalization on January 2, 2009 (3)
<u>Water Service Corporation of Kentucky</u>		NA	NA	\$ 4,235 (4)	NA		
<u>Based Upon the Proxy Group of Seven AUS Utility Reports Water Companies</u>						197.5 % (5)	\$ 8,364 (6)
<u>Based Upon the Proxy Group of Ten AUS Utility Reports Gas Distribution Companies</u>						193.1 % (7)	\$ 8,178 (8)
<u>Proxy Group of Seven AUS Utility Reports Water Companies</u>							
American States Water Co.	NYSE	17,231	\$ 17,534	\$ 302,129	\$ 34,180	194.9 %	\$ 588,956
Aqua America, Inc.	NYSE	133,400	7,319	976,298	20,980	266.7	2,798,732
California Water Service Group	NYSE	20,665	18,664	385,709	45,860	245.7	947,743
Middlesex Water Company	NASDAQ	13,246	10,054	133,178	17,320	172.3	229,421
SJW Corp	NYSE	18,362	12,903	236,934	29,410	227.9	540,026
Southwest Water Company	NASDAQ	23,802	6,669	158,736	3,370	50.5	80,213
York Water Company	NASDAQ	11,265	5,972	67,272	12,220	204.6	137,657
<u>Average</u>		<u>33,996</u>	<u>\$ 11,302</u>	<u>\$ 322,894</u>	<u>\$ 23,334</u>	<u>197.5 %</u>	<u>\$ 760,393</u>
<u>Proxy Group of Ten AUS Utility Reports Gas Distribution Companies</u>							
AGL Resources, Inc.	NYSE	76,400	\$ 21,741	\$ 1,661,000	\$ 31,620	145.4 %	\$ 2,415,768
Delta Natural Gas Company	NASDAQ	3,277	16,609	54,428	24,880	149.8	81,532
Laclede Group, Inc.	NYSE	21,646	19,788	428,325	46,810	236.6	1,013,249
New Jersey Resources Corp.	NYSE	41,611	15,496	644,797	39,230	253.2	1,632,400
NICOR Inc.	NYSE	45,130	20,944	945,200	35,060	167.4	1,582,258
Northwest Natural Gas Company	NYSE	26,407	22,522	594,751	43,590	193.5	1,151,081
Piedmont Natural Gas Co., Inc.	NYSE	74,208	11,837	878,374	31,280	264.3	2,321,226
South Jersey Industries, Inc.	NYSE	29,607	16,249	481,080	39,940	245.8	1,182,504
Southwest Gas Corporation	NYSE	42,806	22,980	983,673	25,300	110.1	1,082,992
WGL Holdings, Inc.	NYSE	49,316	19,887	980,767	32,770	164.8	1,616,085
<u>Average</u>		<u>41,041</u>	<u>\$ 18,805</u>	<u>\$ 765,240</u>	<u>\$ 35,048</u>	<u>193.1 %</u>	<u>\$ 1,407,909</u>


NA = Not Available

- Notes: (1) Column 3 / Column 1  
(2) Column 4 / Column 2  
(3) Column 5 \* Column 3  
(4) From Schedule A of the Company's Petition.  
(5) The market-to-book ratio of Water Service Corporation of Kentucky on December 1, 2008 is assumed to be equal to the average market-to-book ratio at January 2, 2009 of the proxy group of seven AUS Utility Reports water companies  
(6) Water Service Corporation of Kentucky's common stock, if traded, would trade at a market-to-book ratio equal to the average market-to-book ratio at January 2, 2009 of the proxy group of seven AUS Utility Reports water companies. 197.5%, and Water Service Corporation of Kentucky's market capitalization on January 2, 2009 would therefore have been \$8,364 million. (\$8,364 = \$4,235 \* 197.5%)  
(7) The market-to-book ratio of Water Service Corporation of Kentucky on January 2, 2009 is assumed to be equal to the average market-to-book ratio at January 2, 2009 of the proxy group of ten AUS Utility Reports gas distribution companies.  
(8) Water Service Corporation of Kentucky's common stock, if traded, would trade at a market-to-book ratio equal to the average market-to-book ratio at January 2, 2009 of the proxy group of ten AUS Utility Reports gas distribution companies, 193.1%, and Water Service Corporation of Kentucky's market capitalization on January 2, 2009 would therefore have been \$8,178 million. (\$8,178 = \$4,235 \* 193.1%)

Source of Information: 2007 Annual Forms 10K  
yahoo finance.com



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 423-854-5046

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THE DAILY NEWS | THURSDAY | AUGUST 6, 2009

# Bell County public records

PINEVILLE — The following people were recently arrested and lodged in the Bell County Detention Center:

Kathy England, 55, of Middlesboro was arrested on July 14 and served a warrant for other police agency.

Tina Marie Doane, 32, of Middlesboro was arrested on July 14 for operating a motor vehicle while under the influence of alcohol/drugs/etc... and failure to register transfer of motor vehicle.

Michael R. Johnson, 38, of Middlesboro was arrested on July 14 for 1st degree assault and 4th degree assault (domestic violence) with minor injury.

Mark Allen Edmonds, 38, of Shawanee, Tenn., was arrested on July 14 for theft by unlawful taking/shoplifting.

Anna M. Bowling, 32, of Middlesboro was arrested on July 14 and served a bench warrant for court

James Bradley Burke, 26, of Middlesboro was arrested on July 15 for 2nd degree indecent exposure.

Brandon G. Basinger, 24, of Barbourville was arrested on July 15 and served three warrants for other police agency.

Ronnie W. Gambrel, 38, of Flat Lick was arrested on July 15 and served a warrant for other police agency.

Stewart T. Bryant, 50, of Stoney Fork was arrested on July 16 and served three warrants for other police agency.

William M. Vaughn, 18, of Pineville was arrested on July 16 for a misdemeanor probation violation.

Monola Ann Miller, 41, of Arjay was arrested on July

the proposed rate increase sounded "absurd" unless it could be justified.

"That sounds like robbery to me," Brock said.

Middlesboro Mayor Ben Hickman would not comment because he said he was not familiar enough with the matter. Council member Ronnie Carter would not comment, citing the same reason. A message left for Council member Rob Lincks was not returned.

PSC Communications

the PSC would likely decide by the fall.

Clinton, Kentucky in

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**Public Notice**  
 The Public Service Commission will hold a public hearing in Case No. 2008-00563, Application of Water Service Corporation of Kentucky for an Adjustment of Rates, at its office at 211 Sower Blvd., Frankfort, KY 40601 on August 19, 2009 at 10:00 am et for the purpose of cross examination of witnesses and other matters related to the application.

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