

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

INVESTIGATION INTO THE FEASIBILITY OF)
MERCING KENTON COUNTY WATER DISTRICT #1,) CASE NO.
CAMPBELL COUNTY KENTUCKY WATER DISTRICT,) 90-020
AND BOONE COUNTY WATER AND SEWER DISTRICT)

O R D E R

On January 2, 1991, the Commission ordered the performance of full and comprehensive audits of the management effectiveness and operational efficiency of Boone County Water and Sewer District ("Boone District"), Campbell County Kentucky Water District ("Campbell District"), and Kenton County Water District No. 1 ("Kenton District") (collectively "the Water Districts"). By that Order, the Commission also released a revised Request for Proposals ("RFP") and invited comments. The Water Districts were the only parties to submit comments. The Commission addresses their comments herein.

The Water Districts take three general exceptions to the proposed audits. First, they note that they have "undertaken a merger study independent of the Commission" making the Commission's audit "duplicative" and "an unnecessary expense." Water Districts' Response at 2. The record is void of any details on this study. The Commission has yet to be provided information about its scope, financing, or participants. The Water Districts' own comments suggest that funding for the study is

uncertain. Given these unknowns, the Commission does not believe it reasonable to forego or delay its own study.

The Water Districts also contend that they lack sufficient funds to pay for the management audits. They offer no support, however, for this contention. Their decision to perform their own merger study with its associate costs runs counter to this contention. Assuming arguendo that the Water Districts' contention is correct, KRS 278.130(3) makes provision for their recovery of the audit's costs. The Water Districts' lack of funds, therefore, is not an obstacle to the audits.

The Water Districts next reiterate their oft-stated position that KRS 74.361 does not authorize the Commission to impose the cost of any merger study upon them. See e.g., Water Districts' Response to the Commission's Order of May 25, 1990. They "cannot and will not allow the costs of this 'management audit', which is associated with and an integral part of the merger feasibility study under KRS 74.361 and PSC Case No. 90-020 to be passed along to its customers." Water Districts' Response to the Commission's Order of January 2, 1991 at 1-2. They maintain that KRS 278.255 does not "allow management audits to substitute for merger studies, nor does it allow costs associated with merger studies to be funded through a concurrent management audit." Id. at 2.

The Commission does not share this view. It believes that as part of its investigation into the feasibility and advisability of merging certain water districts, it may order management and operation audits as provided in KRS 278.255 to investigate the internal workings of those water districts and to determine

whether merger would improve their management effectiveness and operating efficiency. KRS 278.255 requires the cost of such audits to be borne by the audited water district.

Neither the Commission nor the Water Districts have altered their position in eight months of debate on this point. Continued debate at this level is fruitless. The issue, however, must be resolved. The Commission is without adequate resources to underwrite the costs of the proposed audits or to conduct them itself. Uncertainty over payment of the auditing firm will discourage firms from submitting proposals and ultimately will impact on the quality of any audit.

KRS 418.040 and 418.045 provide a vehicle for resolving this issue before large amounts of money and resources are expended. Accordingly, concurrent with the issuance of this Order, the Commission will petition Franklin Circuit Court for a declaration of its statutory rights and authority under KRS 74.361 and 278.255. Pending a final ruling on that petition, the Commission will hold this proceeding in abeyance.

Having addressed the Water Districts' general exceptions to the proposed audits, the Commission now turns to their comments on specific provisions of the revised RFP. The Commission accepts and has revised the RFP to reflect their request for additional copies of all reports. Additionally, the Commission will alter its internal audit procedures to ensure that the Water Districts receive copies of all monthly status reports with the monthly invoices. Finally, absent the assertion of any applicable

privilege, the Commission will make available upon request the auditing firm's workpapers following completion of the audit.

The Commission rejects the Water Districts' suggestion that they be afforded the opportunity to review invoices prior to Commission approval and to compare the auditing firm's time records with their own. As the Water Districts' records will not reflect such items as travel time and off-site research, the records are not comparable. Furthermore, the Commission finds that the RFP contains adequate safeguards by requiring all invoices to be reviewed and approved by its Management Audit Branch. To further strengthen these safeguards, the letter of agreement between the auditing firm, the Water Districts and the Commission will provide procedures for disputed bills.

Despite the Water Districts' insistence to the contrary, specific provisions in the RFP for their input into the scheduling of interviews are not necessary. Common sense and common courtesy dictate that the auditing firm coordinate with the Water Districts in the scheduling of interviews and on-site visits. The Commission expects all participants to exercise good faith efforts to accommodate the others' schedules.

In their comments, the Water Districts state that they will not commit to implementing the auditing firm's recommendations. They apparently misunderstand the nature of the RFP's action plans. Upon the development of an action plan, a water district will be given the opportunity to agree or disagree with the auditing firm's plan. Where the water district disagrees, it will be required to state the reasons for its disagreement. It, the

auditing firm, and the Commission will then attempt to resolve these disagreements. Where a dispute cannot be resolved, no action will be taken to compel that water district's compliance, absent subsequent independent Commission proceeding. The sole exception concerns the auditing firm's recommendations regarding merger. In that instance, the procedures of KRS 74.361 will be followed.

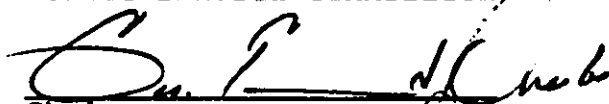
Finally, the Water Districts also suggest that payment provisions of the RFP be modified to not require them to pay for the audit if the audit is terminated prior to completion. As the auditing firm will be incurring expenses in good faith throughout the process, such revision is not justified. The Commission declines to accept it.

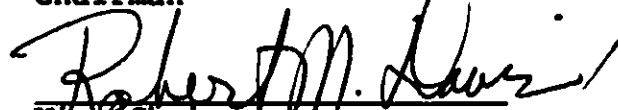
In summary, the Commission finds that this proceeding should be held in abeyance pending a final decision on the Commission's Petition for Declaration of Rights on the issue of cost. If the ruling is in the Commission's favor, then the final RFP, attached as Exhibit A to this Order, should be issued.

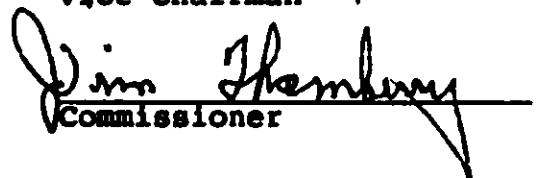
IT IS THEREFORE ORDERED that this case is held in abeyance pending a final decision on the Commission's Petition for Declaration of Rights.

Done at Frankfort, Kentucky, this 8th day of February, 1991.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:


Executive Director

PUBLIC SERVICE COMMISSION OF KENTUCKY

REQUEST FOR PROPOSAL

1. Invitation to Propose

The Public Service Commission of Kentucky ("Commission") is seeking proposals for all consulting services required for the completion of comprehensive management and operations audits of Kenton County Water District No. 1 ("Kenton District"), Campbell County Kentucky Water District ("Campbell District"), and Boone County Water and Sewer District ("Boone District"). The main office locations of these districts are in the northern Kentucky cities of Edgewood, Cold Spring, and Burlington, respectively. Operation of each district is governed by the provisions of the Kentucky Revised Statutes ("KRS") Chapter 74.

The purpose of these audits, which are to be conducted concurrently, will be to review the management and operations of each district. This project will also include a more focused, detailed analysis of and recommendations as to the feasibility and advisability of merger of all or any of the districts.

These audits and merger study are to be performed concurrently. The consultant's final work product should result in the submission of one bound document consisting of an audit report for each district and a report including the consultant's determination regarding the feasibility and advisability of merger.

The Commission in Case No. 90-020, pursuant to KRS 74.361, ordered an investigation of the advisability and feasibility of merger of the Water Districts. KRS 74.361 states the legislative

finding that reduction in the number of operating water districts in the Commonwealth will be in the public interest and that mergers of such districts will tend to eliminate wasteful duplication of facilities and efforts resulting in a sounder and more businesslike degree of management, and ultimately result in greater economies, less cost, and a higher degree of service to the general public, and that public policy favors the merger of water districts wherever feasible.

The Kenton District was organized in 1926. As of December 31, 1989, Kenton District had net utility plant of \$43,979,134 and long-term debt of \$34,561,139. In 1989, Kenton District's total water operating revenues were \$8,452,451 derived from sales of approximately 7.1 billion gallons of water to 31,269 residential, commercial and industrial consumers, and 10 resale customers. Kenton District's total water utility expenses for 1989 were \$5,204,933. Campbell District and Boone District are two of Kenton District's resale customers. Kenton District had a residential customer base of 29,358 consumers at the end of 1989. Kenton District produces its own water using the Licking River and Ohio River as its basic sources. In 1989, Kenton District produced approximately 8.5 billion gallons of water and had a line loss of 16.5 percent.

The Campbell District was organized in 1955 as Campbell County Water No. 1. As of December 31, 1989, Campbell District had \$15,843,273 in net utility plant and long-term debt of \$4,970,800. In 1989, Campbell District's total water operating revenues were \$4,245,947 derived from sales of approximately 1.6

billion gallons of water to 16,138 residential, commercial and industrial customers, 290 public authority customers, 3 resale customers, and fire protection customers. Campbell District's total water utility expenses for 1989 were \$3,168,473. Campbell District had a residential customer base of 15,386 consumers at the end of 1989. Campbell District purchases all of its water from two sources: the Kenton District and the city of Newport. The city of Newport is currently the primary source of supply while the Kenton District is a secondary or supplemental supplier. In 1989, Campbell District purchased approximately 2.0 billion gallons of water and had a line loss of 20.1 percent.

Campbell District is the product of several water district mergers. In 1973, the Mentor Water District and Campbell County Water District No. 3 were merged with Campbell County Water District No. 1. Additionally, in 1975, Campbell County Water District No. 2 was merged with Campbell County Water District No. 1 to form the present Campbell District.

The Boone District was formed in 1952. As of December 31, 1989, Boone District had net water utility plant of \$7,017,250 and long-term debt of \$2,195,000. In 1989, Boone District's total water operating revenues were \$1,518,570 derived, primarily, from sale of approximately 601 million gallons of water to 5,644 residential and 390 commercial customers. Boone District's total water utility expenses for 1989 were \$1,240,695. Boone District purchases all of its water from the Kenton District. In 1989,

Boone District purchased approximately 782 million gallons of water and had a line loss of 22.7 percent.

The Commission believes that such audits are an essential tool of a regulatory agency seeking to protect the interests of utility consumers. The Kentucky General Assembly passed legislation mandating management audits for the Commonwealth's larger utility companies and allowing for management and operations audits of all other utilities under the Commission's jurisdiction. The Commission is currently in the process of performing its first audit of a water utility.

If your firm is interested in proposing to perform this work, you should submit fourteen (14) bound and one (1) unbound, copy-ready copy of your proposal no later than close of business on (INSERT DATE). Any proposal received after this deadline will not be considered. Your response should be addressed to:

Public Service Commission
730 Schenkel Lane
P. O. Box 615
Frankfort, Kentucky 40602

Attention: (INSERT NAME)
(INSERT TITLE), Management Audit Branch

After receipt of proposals, the Commission may request certain firms bidding on the project to appear before the Commission and staff to provide a proposal briefing and to respond to questions. It is anticipated that the project will take 6 months and begin (INSERT DATE). If the bidder thinks additional time is needed, justification should be supplied along with an estimate of additional time.

2. Objectives of the Audits

The objectives of these audits include the determination of what improvements, if any, can be made in the management and operations of the districts -- specifically which, if any, cost-saving measures can be instituted.

The objective of the focused review of the merger issue will be to determine the feasibility and advisability of merger of all or any of the three districts. The Commission, in its Order in Case No. 90-020 recognized the legislative finding in KRS 74.361 and additionally found that sufficient evidence existed in the records of Case Nos. 89-014, 89-029 and 89-179 to indicate that a regionalized water district in northern Kentucky may be advisable. The focused review of the merger issue will provide information to assist the Commission in its determination regarding whether merger is feasible and advisable, and whether merger will provide, both on a short-term and long-term basis, greater economies, better operating efficiencies, and a higher quality of service than would be attainable under the present three district organization.

The ultimate purpose of these audits is to explore all economically practicable opportunities for giving ratepayers the lowest possible rates consistent with good service.

These audits will be broad but comprehensive reviews of the management, its structure and the entire operations of each utility, including a physical inspection of all facilities. While the scope of these reviews will be broad, the depth will be sufficient to determine significant savings, if any, as well as improvements

in management methods or service to Kentucky customers. The quantification of the cost savings associated with audit recommendations should be made whenever possible.

It is expected that the scope of the audit of each district will encompass the following subjects:

EXECUTIVE MANAGEMENT

- Organizational Structure and Planning
- Management Communications and Control
- External Relations

CORPORATE PLANNING

- Strategic Planning
- Water Supply Planning

OPERATIONS PLANNING

- Demand Forecasting
- System Planning and Design
- R & D Functions
- Vendor Selection

ENGINEERING AND CONSTRUCTION

- Quality Assurance
- Operation
- Maintenance
- Projects Management
- Cost Effectiveness

TRANSMISSION AND DISTRIBUTION

- Management
- Operation

TREATMENT AND PUMPING

- Management
- Operation

FINANCIAL SYSTEMS

- Financial Requirements Planning
- Managerial Accounting and Control
- Budget Management and Control
- Economic Analysis
- Internal Auditing
- Rates and Rate Design

CUSTOMER SERVICE

- Meter Reading
- Credit and Collections
- Conservation Programs

HUMAN RESOURCES MANAGEMENT

- Manpower Planning
- Wage and Salary Practices
- Executive Compensation
- Employee Benefits
- Management Development and Training
- Productivity Measurement
- Safety Management

SUPPORT FUNCTIONS

- MIS and Data Processing
- Support Facilities Management and Planning
- Land Management
- Insurance/Claims
- Transportation Management
- Purchasing, Materials Management and Stores
- Legal

In addition, the scope of the focused review of the merger issue should be in sufficient depth to determine if cost efficiencies and improved services will accrue to the customers as a result of merger of all or any of the districts. Further, the qualitative aspects of merger should be examined, including the effect of merger on regional economic development. Both the short-term and long-term consequences of any action must be examined. Quantification of cost efficiencies and service improvements must be provided to support the recommendations of the consultant's report. Qualitative benefits must also be provided. To the extent possible, recommendations concerning the structure of any proposed merger must be supported with specific findings.

The Commission expects that the total consulting fees and expenses for this project will be between \$225,000 and \$325,000.

3. Role of Commission and Staff

The consultant should realize that the Commission is the principal client. Therefore, it is necessary that the Commission maintain control of this engagement. The Commission has

established a Management Audit Branch. (INSERT NAME) of the Management Audit Branch will be the Staff Project Officer designated by the Commission to ensure satisfactory and timely performance of the proposed work. (INSERT NAME) will be the sole contact for the consultant in any discussions with the Commission.

The consultant will be responsible for including the members of the Management Audit Branch and other Commission personnel in the planning and organization meetings and will include members of the Management Audit Branch in all stages of the management audit as directed by the Staff Project Officer. Individual Commission staff members participating in the audits will not function in an advisory capacity to the Commission in any merger investigation arising from recommendations in this report.

The Commission will rely upon the Staff Project Officer to answer questions from time to time about the project and the management and operations of the subject utilities. It will be necessary, therefore, that the Staff Project Officer, Management Audit Branch, and other Commission personnel be involved in the work of the management consultants. This may include attending selected interviews, reviewing analytical procedures, and monitoring the study's progress as to scope, budget, work plans, time, etc. In any event, it is expected that the consultant will frequently discuss his/her progress informally and directly with the Staff Project Officer. The consultant's willingness to work with the Staff Project Officer in the described manner should be stated in the proposal.

The consultant shall include in the proposal an estimate of the amount of time to be spent on-site during the audits. A schedule should be included in the proposal to identify on-site hours for each task area. The Commission expects that a majority of the total hours by the consultant will be spent on-site to allow the Management Audit Branch to effectively maintain control of the engagement. The Commission expects that the consulting firm will have a Project Manager on-site for the majority of this project.

In order to be kept apprised of the project's progress, periodic oral and written reports will be necessary in addition to the informal contact between the consulting staff and the Staff Project Officer. These reports are described below.

Weekly Informal Reports: By the first of each week, the consultant will provide notice of the interviews and site visits scheduled for the next following week to the Staff Project Officer for review and approval.

Monthly Written Status Reports: Based on the task plan submitted with the proposal, the monthly written reports should consist of two parts:

1. General narrative briefly describing progress to date and outlining reasons for any discrepancies between the task plan schedule and progress to date. This narrative should also contain a statement indicating the status of the project in relation to time--ahead, behind, or on schedule.
2. Status sheet indicating actual hours logged by category (i.e., project manager, senior analyst or auditor, junior analyst or auditor, etc.), in each functional area or special interest area by consultant, material and supplies cost, and other costs, showing percentage of each in relation to proposal costs.

Monthly reports (in triplicate) should be in the hands of the Staff Project Officer by the tenth working day following the month's end and shall be submitted for any month worked.

Interview Summaries: By the fifth working day after each interview, formal summaries of each interview, including participants, conclusions/observations, data requests generated and follow-up required, shall be forwarded to the Staff Project Officer. These summaries shall become part of the working papers of these audits.

Interim Written Status Reports: The consultant shall include in the proposal provision for other interim written status reports consistent with the overall project design.

4. Contractual Arrangement

The contract for this project will be between the Commission, the districts and the consultant. Payments to the consultant on a contract entered into as a result of this RFP will be based upon hours actually expended on this project at rates quoted in the proposal. Total payments under this contract will not exceed the total cost quoted in the proposal. Total cost includes itemized cost of supplies and materials, cost of transportation and per diem expenses, and subcontract cost. Fifteen percent (15%) of the total cost of the project will be withheld until delivery of a copy of the final report document, accepted by the Commission, and the draft action plans, to the Commission. Work under this contract is not to be subcontracted without the prior written consent

of the Commission. Neither the rights nor duties of the consultant under this contract are to be assigned without the written consent of the Commission. Neither the Commission nor the districts are liable for any costs incurred prior to the issuance of the contract, including such costs incurred by the successful bidder.

The Commission expects that these audits will be completed in a timely manner. While it is expected that this project will be completed within 6 months, the audits shall be completed no later than 8 months from the start date unless mutually agreed upon by the Commission and the consultant. If the study's completion is delayed beyond 8 months without mutual agreement by the Commission and the consultant, the consultant shall forfeit 10 percent of the total cost of the project.

All invoices shall be presented to the Staff Project Officer by the 10th of the month for services provided in the previous month. The Staff Project Officer shall review and approve all invoices. The invoices will then be forwarded to the districts for payment to the consultant within 10 working days of receipt of same.

Because each audit will be conducted concurrently, the consultant will be required to account for the costs directly assignable to each district. For the purposes of this project, for each applicable monthly payment, each district will be charged and will be required to pay the costs directly assignable to the district and one-third of the common, joint or indirect costs. At the conclusion of the project, the consultant will be required to

submit a final invoice showing the total amount of directly assignable costs charged to each district, and allocating the common, joint or indirect costs to each district based upon their respective proportion of direct costs charged to each district. The amounts previously paid by each district will be reviewed in order to true-up the final amount due from each district.

In case of termination for reason other than fault of the consultant, the consultant shall be paid all monies due for services rendered up to the termination date, as well as all monies due for commitments which cannot be terminated at such termination date or be otherwise mitigated. If the termination is due to the fault of the consultant or his failure to comply with terms of this contract, he shall be entitled to compensation only for such work that has been completed to date and is accepted by the Commission.

It is the intent of the Commission to ensure that any consulting firm, or any of the employees of such a firm who are in a position to directly affect the outcome of the report or services rendered under this contract, shall during the course of the contract, be in strict compliance with the following provisions concerning conflict of interest:

A. Solicitation or Acceptance of Gifts or Favors:

No firm or employee (as referred to above) shall solicit or accept anything of value to the recipient, including a gift, loan, reward, meal, promise of future employment, favor, or service from employees or representatives of the business entities (or any of their affiliates) which are the subject of this contract.

B. Conflicting Employment or Contractual Relationship:

No firm or employee (as referred to above) shall have or acquire any employment or contractual relationship with the business entities (or any of their affiliates) which are the subject of this contract. It is further required that any such relationship (held or acquired during the course of this contract) with any other business entity, which is subject to the regulation of this Commission, shall be discussed with this Commission as to the timing and subject of such relationships. The consulting firm selected shall certify that it will not perform subsequent work for these companies (or any of their affiliates) for a period of two years following the completion of the project without prior permission of the Commission.

C. Disclosure or Use of Certain Information:

No firm or employee (as referred to above) shall disclose or use any proprietary information concerning operations of the business entities being audited, which has been gained by reason of its/his official position as a representative of this Commission and which is not available to the general public, for corporate or personal gain or benefit, or for the gain or benefit of any other business entity or person, without the necessary written approval.

D. Disclosure of Specified Interests:

If any firm or employee (as referred to above) holds any interest (other than paragraph B above) or owns or acquires a material financial position in the net worth of the business entities under review, a statement shall be filed disclosing such facts prior to signing any contract with this Commission, or immediately upon the establishment of such an interest, if such takes place during the course of a contractual obligation to this Commission.

E. Corporate Conflict of Interest Policy:

All consulting firms desiring to do business with this Commission must submit, as part of their proposal or potential contract, a copy of their Corporate Conflict of Interest Policy, particularly in regard to stock ownership and/or financial relationships with clients. In the case of non-incorporated consultants or where no corporate policy exists, a statement of intention to comply with the preceding provisions must be submitted.

5. Contents of Proposal

Consultant's proposals should include the following:

A. STATEMENT OF THE PROJECT

State in succinct terms your understanding of the project presented in this RFP.

B. MANAGEMENT SUMMARY

Include a narrative description of the proposed effort, a discussion of project management practices, and a list of the end products that will be delivered, including the final report document.

C. WORK PLAN

Task descriptions are to be the guide in describing your technical plan for accomplishing the work. The task descriptions should be in sufficient depth to afford the Commission and staff a thorough understanding of your work plan. The description should include an estimate of the number of hours each primary member of the auditing team will devote to each task, functional area, and special interest area. Consultants are cautioned that their proposals may be rejected if their work plan does not specifically detail how each of the task descriptions is to be accomplished.

D. PRIOR EXPERIENCE

Submit a statement of similar management audits conducted in the previous 5 years. Provide a copy of the most recently completed audit report. This would also apply to a subcontractor if appropriate. Indicate specifically any management audits of utilities and provide copies of such audit reports. Experience shown should be work done by your company rather than by individuals. Studies or projects referred to should be identified and the name of the client shown, including the name, address and phone number of the responsible official of the client company or agency who may be contacted.

E. PERSONNEL

Include the names of all personnel--executive, professional, management analysts, systems analysts, auditors, staff consultants, etc.--who will be engaged in the work. Their education and experience in auditing and management evaluations, especially for utilities, must be included.

F. STATEMENT ON POTENTIAL CONFLICTS OF INTERESTS

The consultant shall identify any relationships between itself and/or any of its affiliated companies (including prior relationships of individual personnel to be performing the work) and the districts to be audited. This would include any work done during the last five years for the districts. If there have been no such relationships, a statement to that effect is to be included in the proposal. If, during the audit, it is determined that an undisclosed conflict has or had existed between the consultant and the districts, the Commission reserves the right to terminate the contract.

G. BUDGET ESTIMATES

For each task described in C above, a cost estimate shall be provided. The cost estimate for each task shall include manpower costs, costs of supplies and materials, subcontractor costs, transportation costs and total cost. The manpower costs should be broken down to identify the category of personnel, estimated hours, rate per hour and total cost. A firm maximum cost for the proposal shall also be provided.

H. TIME ESTIMATES

For each task described in C above, an estimate of the elapsed time required for completion shall be provided. Include a display of the complete schedule of the project showing each event. An estimate of the percentage of time spent on-site shall be provided.

I. INITIAL REQUEST FOR DOCUMENTS

The consultant shall submit an initial information request of pertinent documents as a part of the proposal. Upon final selection of the consultant by the Commission, the audited districts shall initiate responses to the initial information request, thus enabling the consultant to have access to the requested information during the early stages of the audits.

J. WORK SPACE

Requirements for working/office space at the districts' headquarters should be specified in the proposal.

K. SIGNATURES

All proposals must be signed by an official authorized to bind the consultant to its provisions. The successful bidder's proposal and the proposal contents will become contractual obligations of the consultant.

6. Selection Criteria

All proposals received shall be evaluated by the Commission and the Management Audit Branch. To select the proposal which most closely meets the requirements of this request for proposal, consideration will be given to several factors. One factor will be the consultant's understanding of the Commission's needs and a proposed approach that satisfies these needs. Another important factor will be the experience and ability of the consultant's staff assigned to the project and their capability to perform the proposed work. Also, attention will be given to the proposal's description of tasks in the work plan to determine if the consultant possesses the knowledge and understanding of the technical functions to be examined in the audits. Another important factor is the consultant's willingness to include the Management Audit Branch in the various stages of the audit. The Commission will also consider the project management techniques and practices. Cost will be given significant consideration, although it will not necessarily be the deciding factor. Finally, demonstrated ability to meet stated deadlines will also be a consideration.

7. Testimony

The selected consulting firm must be willing to stand behind its conclusions and recommendations by testifying in a proceeding before the Commission at its standard compensation rates. The consultant should designate its witness or witnesses and state its

hourly compensation rate with the proposal. This rate should be firm through (INSERT DATE). Payments to the consultants will be based upon the hours expended at rates quoted in the proposal. Total payments under this section of the contract will be for actual expenses incurred and approved by the Staff Project Officer.

8. Draft/Final Report

It is expected that each final audit report and the merger report will evolve from draft reports due at least 30 days prior to the submission of the final report. The draft audit reports should be comprised of the task reports and recommendations. In addition, all task and draft reports shall be footnoted. Each district, separately, the Management Audit Branch and the consultant will review the findings of each task report at a 3-party roundtable meeting prior to the issuance of each task report. Task reports shall be submitted early enough in the project to allow for additional in-depth analyses and subsequent revisions. Upon review of the task reports, the Management Audit Branch and each district will provide written comments to the consultant so that the consultant can make any changes before completing the final report. Also, each district, the Management Audit Branch and the consultant will review the findings of the merger report at a 5-party roundtable meeting prior to the issuance of a draft merger report. Upon review of the draft merger report, the Management Audit Branch and each district will provide written comments to the consultant so that the consultant can make any changes before completing the final report. The consultant must

address each of the district's comments to the draft audit reports and draft merger report. A final review meeting may be held if necessary.

The Commission requires the final report to be in written narrative form with footnotes and include the following, written in terminology that will be meaningful to the Commission, each district, and intervenors that are generally familiar with the subject areas:

- A. General Statement and Management Summary.
- B. Findings and Conclusions.
- C. Recommendations for immediate changes that management can institute involving potential cost savings. This would include a schedule listing, by priority, the recommendations.
- D. Recommendations as to specific areas that would require in-depth analyses and estimates of time and cost factors involved prior to implementation, if needed.
- E. Findings, conclusions and recommendations regarding merger.

It will be necessary that recommendations, especially those involving significant cost savings, be justified and accompanied by adequate supporting information. In providing adequate supporting information for those recommendations involving cost savings, the consultant should include the following for a specific time period(s):

- Operating costs incurred before implementation of the recommendations.
- Operating costs to be incurred after implementation of the recommendation.
- Cost of implementing the recommendation.
- Savings after consideration of implementation costs.

Although the report should emphasize opportunities for improvement, findings of superior management and operating effectiveness are also encouraged to the extent that they can be documented. The consultant shall be responsible for the development of action plans to implement each recommendation and will be required to review the appropriateness of detailed action steps developed by the districts as discussed below.

The consultant shall provide the Commission with 50 copies and one unbound, copy-ready copy, and each district with 12 copies of the final report document. The final report document is due (INSERT NO.) months from the start of the project.

8. Action Plans

Except for recommendations regarding merger, it is the Commission's intent to secure a commitment from the districts to implement the consultant's recommendations as expeditiously as possible, and to develop a dialogue between the districts and the consultant regarding the proper action steps necessary to successfully implement each recommendation. The process of developing action plans will therefore be expected to include the following events:

A. The consultant will be responsible for developing draft action plans which include the background, the priority, the improvement baseline intended, and the estimated one-time and annual costs and benefits for each recommendation. These draft action plans will be submitted with the final report document.

B. The districts will then be responsible for reviewing the consultant's draft action plans, providing comments regarding the merits of each recommendation and the particulars discussed by the consultant in each action plan, and listing the detailed steps (as well as the start date and completion date for each step) necessary to implement the recommendation.

C. The consultant will then be responsible for reviewing each district's comments and action steps and formally commenting (in the finalized action plan) on the appropriateness of each district's implementation activities, as well as clarifying the intent of the recommendations, if necessary.

D. The consultant shall be responsible for printing the finalized action plans, and shall provide the Commission with 10 bound copies and one unbound, copy-ready copy and each district with 5 bound copies of the finalized action plans.

An example of the action plan format desired by the Commission is attached following page 22 of this RFP.

Because the nature of implementation of audit recommendations could be affected by merger, the consultant will also be required to develop appropriate action plans consistent with the recommendations of the merger report.

9. Work Papers

It is expected that all formal workpapers utilized by the consultant during the course of the project will be available to the Commission during the audits and turned over to the Commission before the end of the project. At a minimum, the working papers should include interview summaries (or a copy of interview notes),

data request responses, and any special analyses prepared by the consultant. An indexed copy of the final report document should be submitted which identifies the source of the information presented for each finding. This will help ensure proper documentation of the final report document and will facilitate the Commission's monitoring of the implementation process.

**KENTUCKY PUBLIC SERVICE COMMISSION
MANAGEMENT AUDIT ACTION PLAN**

I. Recommendation Statement (Consultant)

II. Report Reference (Consultant)

A. Chapter _____

C. Recommendation No. _____

B. Section _____

D. Priority _____

III. Background (Consultant)

(This Section Should Discuss Key Findings And Conclusions, Noting Deficiencies Which Are Addressed By The Recommendation)

IV. Improvement Baseline (Consultant)

(This Section Should Include A Discussion Of The Specific Improvement That Will Exist After The Recommendation Is Implemented)

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V. Cost/Benefit Analysis and Support (Consultant)

A. Cost Analysis:

(This Section Should Address The Costs Associated With Implementing The Recommendation, Along With The Specific Support For The Cost Estimate)

B. Benefit Analysis:

(This Section Should Address The Benefits Associated With Implementing The Recommendation, Along With The Specific Support For The Estimate)

C. Cost/Benefit Summary:

Category	One Time	Annual Recurring
Cost		
Benefits		

D. Other Costs or Benefits:

(Other Costs Or Benefits That Cannot Be Quantified Should Be Described In This Section)

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VI. Responsibility (Company)

A. Name _____

B. Title _____

C. Recommendation Action:

Approved Approved With Exception Rejected

D. Explanation of Exception or Rejection:

(This Section Should Address The Reasons The Company Has Rejected Or Taken Exception To The Recommendation)

VII. Company Response (Company)

A. Discussion of Recommendation:

(This Section Should Address The Company's Interpretation Of The Recommendation)

B. Improvement Proposed by Company:

(This Section Should Include The Company's Perspective On What Improvement Will Be Realized)

C. Discussion of Cost/Benefit Analysis:

(This Section Should Address The Company's Estimate Of The Costs And Benefits Associated With The Recommendation)

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VIII. <u>Implementation Steps</u> (Company)			
No.	Step	Dates	
		Start	Complete
	(The Company Should List The Specific Actions To Be Taken To Realize The Intended Improvement, As Well As A Start And Completion Date For Each Step)		
IX. <u>Comments/Clarification of Intent</u> (Consultant)			
A. Consultant Name _____			
B. Discussion:			
(The Consultant Should Respond To The Company's Discussion, Improvement, Steps, And Cost/Benefits. Included Should Be The Consultant's Perspective, Particularly On Areas Of Disagreement)			