COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF KENTUCKY-AMERICAN WATER COMPANY TO INCREASE ITS RATES	))	CASE NO. 95-554

O R D E R

IT IS ORDERED that Kentucky-American Water Company ("Kentucky-American") shall file the original and 12 copies of the following information with the Commission by May 3, 1996, with a copy to all parties of record. Each copy of the data requested should be placed in a bound volume with each item tabbed. When a number of sheets are required for an item, each sheet should be appropriately indexed, for example, Item 1(a), Sheet 2 of 6. Include with each response the name of the witness who will be responsible for responding to questions relating to the information provided. Careful attention should be given to copied material to ensure that it is legible. Where information requested herein has been provided along with the original application, in the format requested herein, reference may be made to the specific location of said information in responding to this information request. When applicable, the information requested herein should be provided for total company operations and jurisdictional operations, separately.

1. Provide the allocated 1996 pension cost for American Water Works Company ("American Water Works") including the annualized rate of valuation earnings, the allocation percentage,

and the allocated pension cost. The information should be provided in the same format as W/P-3-7, page 2 of 39.

2. In comparing the present rate base adjustment for the Other Post Retirement Employee Benefits ("OPEBs"), W/P-1-13, page 1 of 2, to the same adjustment in Case No. 94-197,[1] W/P-1-12, the prior adjustment used the expense vs. capitalization rate of 86 percent from Case No. 92-452,[2] while the present adjustment uses an expense rate of 88.67 percent. Explain why the expense rate of 86 percent from Case No. 92-452 was not used to compute the adjustment in this case.

3. In Case No. 94-197, Kentucky-American projected increases in group insurance premiums of 7.5 percent in October 1994 and October 1995. Apparently, neither increase materialized since Grubb Direct Testimony, page 12, states that the current group insurance premiums have been in effect since January 1, 1994. In light of this previous inaccuracy in projecting insurance increases, provide all available documentation to substantiate the 2.5 percent increase projected for group insurance premiums effective January 1997.

4. In its response to Item 72 of the Commission's Order dated March 13, 1996, Kentucky-American indicated that it does not agree with the actuarial assumptions it was asked to make. Does

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1 Case No. 94-197, Notice of Adjustment of the Rates of Kentucky-American Water Company.

2 Case No. 92-452, Application of Kentucky-American Water District for an Adjustment of Rates.

Kentucky-American contend that the health care cost trend rates American Water Works selected for its actuarial study are the only reasonable rates that could be used to determine SFAS 106 costs? Thoroughly explain your answer.

5. Isn't it true that the health care cost trend rates are estimates and that an independent actuary reviewing information on Kentucky-American's plan for postretirement benefits other than pensions might very well determine a different set of rates to be more appropriate than those selected by American Water Works for determining its 1995 SFAS 106 costs?

6. According to Kentucky-American's response to Item 137 of the Attorney General's data request No. 1, the projected 1996 OPEB expense reflects a health care cost trend rate of 9 percent for 1996. Isn't this an indication that the trend rates in the 1995 report were too high since it projected the 1996 rate to be 10 percent?

7. Refer to Kentucky-American's response to Item 1(b) of the Commission's Order dated March 13, 1996:

a. Actual OPEB expense was reported to be $80,282 lower than anticipated. Explain in detail the reason the OPEB forecast was overstated.

b. The actual pension expense was reported to be $84,491 less than the amount projected. According to the variance analysis, the pension expense was based on the 1995 forecast for the American Water Works which was $2.5 million higher than the actual cost. Explain in detail the reason the pension expense was overstated.

c. What assurance can Kentucky-American provide that the current forecasts of OPEB and pension expenses are more accurate than the previous forecasts?

8. Explain the basis for allocating the related costs of production for leak adjustment to all classes of customers as opposed to allocating the costs only to residential and commercial customers.

9. Explain why Kentucky-American does not bill the Lexington-Fayette Urban County Government for water used for street sweeping.

10. Does Kentucky-American propose to change its proposed capital structure and rate of return based on a slippage adjustment? If so, what is its new proposal?

11. In regard to the variances in proposed and actual capital structure set out in Kentucky-American's response to Item 1 of the Commission's Order dated March 13, 1996, does Kentucky-American anticipate any such variances from its planned new securities issuances as discussed in Tillotson Direct Testimony, pp. 5-6?

12. Refer to the response to Item 1 of the Commission's March 13, 1996 Order. In Case No. 92-452,[3] Kentucky-American's proposed rate base exceeded its actual rate base by $2,902,120. Can the majority of the variance between the forecasted and actual rate

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[3] Case No. 92-452, Order Dated November 19, 1993.

base be attributed to construction delays? If no, explain the reason for the variance.

13. Refer to the response to Item 3 of the Commission's March 13, 1996 Order. Since approximately 58 percent of the construction projects started or completed between January 1, 1986 and December 31, 1995 were started or completed behind schedule, explain how the investment budget schedule presented by Kentucky-American should be considered realistic and reliable.

14. Refer to the response to Item 4 of the Commission's March 13, 1996 Order:

a. Explain why budget project 90-13, the Kentucky River Aquatic Study, was concluded in 1991 but is still reported in Construction Work In Progress ("CWIP").

b. Explain why budget project 90-13, the Kentucky River Aquatic Study, is not accruing AFUDC.

c. Describe the relationship between budget project 90-13, the Kentucky River Aquatic Study and budget project 92-12, Develop Additional Source of Supply.

d. Explain why Kentucky-American has not combined budget project 90-13, the Kentucky River Aquatic Study, with budget project 92-12, Develop Additional Source of Supply.

15. Stockton Direct Testimony, p. 14, states that every year a major highway reconstruction project has occurred. In Case No. 92-452, Kentucky-American included a major highway reconstruction in its forecasted operations, but in the response to Item 1 of the Commission's March 13, 1996 Order Kentucky-American admitted that

a highway relocation did not occur during that period. Explain the contradiction between Stockton's testimony and what occurred in Case No. 92-452.

16. Given that the highway relocation project in Case No. 92-452 did not occur, explain why this project should be included in the forecasted operations.

17. Has the Lexington-Fayette County Government or the Commonwealth of Kentucky approached Kentucky-American about possible highway relocations that will occur in the forecasted test period? If yes, provide a description of each highway relocation and cost estimate for each project.

18. The response to Item 6 of the Commission's March 13, 1996 Order shows that 4 of the 6 highway relocation projects completed between 1990 and 1995 cost under $150,000. Given this past history, explain how Kentucky-American arrived at its projected highway relocation cost of $200,000.

19. Refer to the response to Item 13 of the Commission's March 13, 1996 Order:

a. Kentucky-American states that feasibility studies are charged to CWIP because the report and control features of its work order investment budget control system allow it to review and control the overall cost of the study. Explain why Kentucky-American cannot implement the same control system for Account 183 - Preliminary Survey & Investigation that is used to monitor CWIP.

b. When a feasibility study is undertaken and reported in CWIP, does Kentucky-American accrue AFUDC on the cost of the study?

c. Does the cost of a feasibility study transferred from CWIP to Account 183 - Preliminary Survey & Investigation continue to accrue AFUDC?

d. Kentucky-American states that a feasibility study should be included in CWIP because it is for basic design work that Kentucky-American does not consider to be preliminary in nature. Explain why basic design work for a project that has yet to be granted a Certificate of Public Convenience and Necessity ("Certificate") is not considered preliminary in nature.

e. If the feasibility study is not considered preliminary in nature when it is being undertaken, explain why the nature of the study would change at its conclusion, allowing the cost to be transferred to Account 183.

20. Refer to the response to Item 14 of the Commission's March 13, 1996 Order. The uncertainty of construction was one of the criteria the Commission cited in removing the cost of the Ohio River supply line from rate base in Case No. 92-452. Isn't the construction still uncertain, given the ongoing studies of the Kentucky River and the absence of a Certificate authorizing any construction?

21. Kentucky-American refers to a Kentucky River Authority revision to a HARZA study to evaluate the environmental impact of seasonal increases in the dam heights at pools 9 and 10.

a. Is this a new study or a revision to the original HARZA study?

b. When did HARZA begin the study?

c. When is the study scheduled to be completed?

d. Provide any information or correspondence Kentucky-American has had with the Kentucky River Authority regarding this study.

22. Kentucky-American states that it should proceed with the source of supply project design at the conclusion of the University of Kentucky and HARZA studies. Is it premature for Kentucky-American to include the design cost of the Ohio River supply line in rate base before the studies have concluded?

23. If the preliminary design and easements costs of the Ohio River supply line are excluded from rate base until issuance of a Certificate to construct, explain how Kentucky-American's future plans for this project will be affected.

24. If a construction project requires a Certificate, is the cost of the Certificate case included in rate base as a separate item or is it combined with the construction project?

25. Refer to the response to Item 15 of the Commission's March 13, 1996 Order:

a. Kentucky-American states that Case No. 93-434[4] relates to the Commission's and Attorney General's investigation into the source of supply issue. Since the purpose of that case

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[4] Case No. 93-434, An Investigation of the Sources of Supply and Future Demand of Kentucky-American Water Company, Order dated April 24, 1995.

was to investigate Kentucky-American's demand and sources of supply, explain why the cost of this proceeding should not be combined with budget project 92-12, Develop Additional Source of Supply.

b. Does the requested rate of return on equity reflect some level of risk to the shareholder's investment?

c. Would allowing the shareholder to recover the carrying cost for preliminary investigations, before a Commission decision to construct or abandon the project, reduce the investment risk and lower the required return on equity?

26. In response to Item 16 of the Commission's March 13, 1996 Order, Kentucky-American plans to begin design and easement work in April 1997 in preparation of a Certificate application. Provide the date Kentucky-American intends to file for its Certificate to construct the Ohio River supply line.

27. Refer to the response to Item 19 of the Commission's March 13, 1996 Order:

a. The response to Item 1 of the Commission's March 13, 1996 Order shows that Kentucky-American's forecasted Utility Plant in Service ("UPIS") and UPIS adjusted by the slippage factor exceeded the actual UPIS level by $4,354,213 and $2,684,176, respectively. Given that Kentucky-American's rates were based on a higher level of UPIS investment than was actually incurred, explain why the Commission's method would not be considered conservative.

b. In Case No. 94-197, Kentucky-American's forecasted UPIS and UPIS adjusted by the slippage factor exceeded the actual UPIS level by $3,568,356 and $1,163,224,[5] respectively. Given that in both rate cases the UPIS adjusted for slippage is more accurate than Kentucky-American's budgeted amounts, explain why the Commission's use of the ten-year average of construction is inappropriate.

c. Kentucky-American states that the events leading up to the Jacks Creek Pipeline were unusual in that Kentucky-American never experienced them before and that nothing would indicate that any project in its forecasted test year will match the unusual events of Jacks Creek. Explain how the Ohio River supply line compares to the Jacks Creek Pipeline.

d. When Kentucky-American prepared its construction budget for the Jacks Creek Pipeline, was there any indication of the possible delays and cost increases that would be involved?

e. Is it always a possibility that utility construction projects that require a Certificate may be delayed beyond the time budgeted for the projects?

f. Provide copies of all assumptions, workpapers, and calculations used to arrive at the capital structure contained on page 4 of 16.

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5 Case No. 94-197, response to Item 23 of the Commission's August 4, 1994 Order.
$162,079,573 UPIS - $923,024 Source of Supply = $161,156,549 UPIS Adjusted for Slippage - $159,993,325 Actual UPIS = $1,163,224.

28. Refer to the response to Item 26 of the Commission's March 13, 1996 Order:

a. Provide a comparison of the income that is generated by the over-funding of OPEBs with the revenue effect of including the overfunded OPEBs in rate base. Include all assumptions, workpapers, and calculations used in the comparison.

b. Since the Joint Stipulation in Case No. 94-197 contained only the revenue amount agreed upon, how did Kentucky-American make the assumption that the "stipulation recognized the full amount of OPEBs"?

29. Refer to the response to Item 27 of the Commission's March 13, 1996 Order. In the past the Commission has decided that deferred costs that benefit both the ratepayers and stockholders should be borne by both and has excluded the unamortized cost from rate base. Explain why these deferred costs should not be given that same treatment.

30. Refer to the response to Item 33 of the Commission's March 13, 1996 Order:

a. The 1995 comparisons of the budgeted to actual expenses were not included in the response to Item 4 of the Commission's January 30, 1996 Order. Provide the requested expense comparisons and variance explanations as originally requested.

b. The comparison of management fees was not included in the response to Item 74 of the Commission's August 4, 1994 Order in Case No. 94-197. Provide the requested comparison for

Management fees for the period 1986 through 1995. Describe and explain any variance which exceeds 5 percent.

c. Based on the information contained in the response to Item 4 of the Commission's January 30, 1996 Order, the Commission was unable to make the 1994 comparisons for the following expenses. Provide the comparisons requested for 1994 for these expenses:

(1) Customer Accounting Expense

(2) Miscellaneous Expense

(3) Maintenance Expense

31. Refer to the response to Item 39 of the Commission's March 13, 1996 Order:

a. Kentucky-American has calculated a revised test-year cost of $15,912 to haul sludge. Does this revision reflect the delay in hauling sludge from the Kentucky River Station? If not, explain the reason for the adjustment and how it was determined.

b. If the reason is for a delay in hauling sludge from the Kentucky River Station, provide an explanation for the delay.

32. Refer to the response to Item 40 of the Commission's March 13, 1996 Order:

a. Based on the information contained in the response to Item 4 of the Commission's January 30, 1996 Order, the Commission was unable to develop the 1994 and 1995 comparisons for programmed maintenance. Provide the comparisons requested for 1994 and 1995 and describe any variance that exceeds 5 percent.

b. For the period of 1986 through 1994 the ratio of actual to budgeted programmed maintenance was 82.673 percent. Explain why Kentucky-American's forecasted programmed maintenance should not be adjusted to reflect this historical ratio.

c. Given the low ratio of actual to budgeted program maintenance for the period of 1986 through 1994, provide all available documentation to demonstrate that the forecasted programmed maintenance is realistic and reliable.

33. Refer to the response to Item 47 of the Commission's March 13, 1996 Order:

a. Since the accounting transactions remain stable from year to year, has the American Waterworks Service Company ("Service Company") consider using the transactions as the allocator for the accounting function? Explain your response.

b. Is stability a major criteria that should be considered when choosing an allocation method?

34. Refer to the response to Item 48 of the Commission's March 13, 1996 Order:

a. Is the response to this question "no" regarding the performance of studies to look at each cost separately to identify its underlying characteristics?

b. Explain why all costs including labor and overhead costs should not be included in the direct billed charges.

35. Refer to Exhibit 37, Schedule F-6, Rate Case Expense. The actual accounting expense incurred in Case Nos. 94-197 and 92-452 were $120,744 and $153,623, respectively. Explain why Kentucky-

American forecasted its rate case accounting expense would increase to $215,000.

36. Refer to the response to Item 53 of the Commission's March 13, 1996 Order:

a. The references cited by Kentucky-American contain only totals and do not have the details to show how the amounts were derived. Provide the details showing how each of the costs were derived.

b. Provide the actual rate case costs incurred to date, broken down by the categories listed in the references.

37. Refer to the response to Item 55 of the Commission's March 13, 1996 Order. The comparison of actual to budgeted insurance other than group insurance expense was not included in the response to Item 74 of the Commission's August 4, 1994 Order in Case No. 94-197. Provide the requested comparison for the period 1986 through 1995. Describe and explain any variance which exceeds 5 percent.

38. Refer to the response to Item 57 of the Commission's March 13, 1996 Order:

a. In what year did Kentucky-American expense the cost to move Roy Mundy to Lexington?

b. For rate-making purposes, the Commission considers a cost that was expensed and paid in the year incurred to have been recovered from ratepayers. Explain why Kentucky-American's ratepayers should now pay for a non-recurring cost that has already been expensed and paid.

39. Refer to the response to Item 63 of the Commission's March 13, 1996 Order. Since the temporary meter readers will be used only in the transition period, explain why the cost should not be considered nonrecurring and amortized over an appropriate period.

40. Refer to the response to Item 66 of the Commission's March 13, 1996 Order. Recalculate the increase in transportation cost due to monthly meter reading using the 2.5 percent inflation factor.

Done at Frankfort, Kentucky, this 17th day of April, 1996.

PUBLIC SERVICE COMMISSION

Linda K Breathitt

For the Commission

ATTEST:

Don Mills

Executive Director