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

ORDER

IT IS ORDERED that Intervenor Chetan Talwalker shall file the original and 9 copies of the following information with the Commission with a copy to all parties of record no later than June 17, 1996. Careful attention should be given to copied material to ensure that it is legible.

1. Given the current customer usage information that is available, provide the method in which you would determine a seasonal or inclining block rate.

2. What considerations would you give to off peak usage periods for customers who use large quantities of water?

3. What conservation message or price signal will customers receive if a seasonal or inclining block rate is implemented prior to monthly billing?

4. If the costs associated with the pipeline were to be recovered through a monthly surcharge based on water usage (surcharge per 1,000 gallons), what subsidies would occur?

5. Is it your testimony that the costs associated with the pipeline should be collected through either seasonal or inverted rates?

6. Is it your opinion that the implementation of a seasonal or inclining rate block will result in the elimination of the need for the pipeline?

Done at Frankfort, Kentucky, this 5th day of June, 1996.

PUBLIC SERVICE COMMISSION

Linda K Breathitt

For the Commission

ATTEST:

Don Mills

Executive Director

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

ORDER

IT IS ORDERED that the Attorney General, by and through his Public Service Litigation Branch, shall file the original and 9 copies of the following information with the Commission with a copy to all parties of record no later than June 17, 1996. Careful attention should be given to copied material to ensure that it is legible.

1. The direct testimonies of Bruce E. Tillotson and Paul R. Moul indicate that Kentucky-American Water Company ("Kentucky-American") is proposing the capital structure detailed on Exhibit 37, Schedule J-1.1/1.2, page 1 of 1. This page indicates a proposal to include short-term debt at a level of .557 percent. Dr. Weaver states on page 8 of his testimony that Mr. Tillotson's recommended capital structure does not contain short-term debt. Did Dr. Weaver intend to use Kentucky-American's proposed capital structure elements, including $118,809,600 in total capital, in calculating his recommended capital structure?

a. If yes, recalculate the capital structure recommended in Schedule 17.

b. If no, explain why capital components as of August 31, 1997 were used instead of Kentucky-American's proposed 13 month average components.

2. Refer to Dr. Weaver's testimony, Schedule 17, page 1. Explain the calculation of the assumed actual reductions in Column 4.

3. Why did Dr. Weaver not use Kentucky-American's proposed short-term debt rate of 6.45 percent in calculating his recommended cost of capital?

4. Refer to page 66 of Dr. Weaver's testimony, which indicates a range of DCF cost of equity results of 7.8 percent to 12.7 percent. Explain the conclusion that the results indicate a cost of equity of between 9.1 percent and 10.3 percent.

5. Refer to Carl Weaver's Testimony Schedule 17, page 2, Percent of Short-Term Debt:

a. The AG/LFUCG states that the Average Daily Short-term Debt Column was obtained from Kentucky-American's Exhibit 37, Schedule J-1, Page 1, The Overall Financial Summary as of August 31, 1997. Explain how the average daily short-term debt totals for the period of 1989 through 1994 were obtained from this exhibit.

b. On this schedule the AG/LFUCG shows that Kentucky-American's 1994 long-term debt is $51,000,000; however Exhibit 28 of the Filing Requirement, page 7 reveals that the 1994 long-term debt is $57,000,000. Explain the discrepancy between these two numbers.

c. Explain why 1995 is not reflected in the AG/LFUCG's analysis.

d. The schedule lists long-term debt of 3.53 percent and then states that short-term debt percent is 3.5 percent. Provide the calculation of long-term debt of 3.53 percent, and explain the relations ship between the two statements.

6. The AG/LFUCG proposed to revise Kentucky-American's capital structure to include short-term debt of $4.2 million. Explain how the AG/LFUCG arrived at its proposed

level of short-term debt of $4.2 million. Include in the explanation all assumptions, calculations, and workpapers.

7. To offset the increase to short-term debt, the AG/LFUCG proposed to reduce long-term debt, preferred stock, and equity by amounts to maintain their proportionate relationship in the capital structure. Explain why the AG/LFUCG proposed to keep the same proportionate relationship as posed by Kentucky-American.

8. The AG/LFUCG has stated that an increase to short-term debt will impact the amount of outstanding preferred stock. Explain how a change in the level of short-term debt would impact preferred stock.

9. The AG/LFUCG reduced Kentucky-American's proposed utility plant in service and rate base to reflect the ratio of actual to budgeted construction spending, labelled the "slippage factor." Is the AG/LFUCG's slippage factor reduction to rate base reflected in its proposed capital structure contained on Schedule 19 of Carl Weaver's Testimony. If, yes show how the capital structure was adjusted. If no, explain why the capital structure was not adjusted.

10. a. In its response to Item 19 of the Commission's March 13, 1996 Order, rate base was reduced by $2,666,317 to reflect the slippage factor adjustment. Kentucky-American reduced its capital structure by an identical amount and, therefore, removed short-term debt of $672,335 and reduced long-term debt and capital by $1,200,000 and $800,000 respectively. Explain the AG/LFUCG's position regarding Kentucky-American's proposed adjustment.

b. Should an adjustment similar to the one proposed by Kentucky-American be made to the AG/LFUCG's capital structure? If no, provide a detailed explanation of why this adjustment would be inappropriate.

11. Refer to the Direct Testimony of Thomas C. DeWard, Schedule 5, Accounts Payable Offset to Rate Base:

a. Explain if the AG/LFUCG's adjustment takes into account changes in AFUDC or property taxes that would result from reductions in CWIP and Utility Plant In Service ("UPIS") balances.

b. The AG/LFUCG calculated the ratio of its claimed accounts payable to CWIP balance which was then applied to Kentucky-American's proposed materials and supplies account to determine an accounts payable offset for materials and supplies. Explain the relationship between CWIP and balances in the materials and supplies accounts.

c. Explain why it is appropriate to use the above ratio in determining an accounts payable offset to the materials and supplies account.

d. Provide all assumptions, calculations, and workpapers used to arrive at the estimated amount for the accounts payable offset for deferred maintenance.

12. Refer to Thomas C. DeWard's Direct Testimony, page 13, C - Remove net Income from Cash Working Capital:

a. The AG/LFUCG has proposed to remove net income from the cash working capital allowance determined from Kentucky-American's lead/lag study. Is the AG/LFUCG aware of any jurisdictions where net income is not included in a lead/lag study?

If yes, provide a list of jurisdictions and include copies of Orders that discuss the disallowance of net income from lead/lag studies.

b. Is the AG/LFUCG aware of any publications or journals that support the AG/LFUCG's position on excluding net income from lead/lag studies? If yes, provide copies of the publications or journals.

13. Refer to Thomas C. DeWard's Direct Testimony, pages 13 and 14, D - Remove Median Service Days from Zero Lag Day Items:

a. The AG/LFUCG claims that Kentucky-American ignores that depreciation and deferred taxes occur ratably over the month. Therefore, the AG/LFUCG has proposed to replace the zero lag days Kentucky-American proposed for these expenses, with revenue lag of 12.87 days. Is the AG/LFUCG aware of any jurisdictions where depreciation and deferred taxes are assigned the revenue lag days? If yes, provide a list of jurisdictions and include copies of Orders that discuss this treatment.

b. Is the AG/LFUCG aware of any publications or journals that support the AG/LFUCG's position on depreciation and deferred taxes? If yes, provide copies of the publications or journals.

14. Refer to Thomas C. DeWard's Direct Testimony, pages 15 and 16, F - Adjust for Rates which Over-Collect Return Requirements:

a. The AG/LFUCG claims that Kentucky-American will over -collect in the early months of the test period because rate base is less than the average amount which rates are predicated. Is the opposite true for the last months of the test period, Kentucky-American will under-collect because rate base will be greater than the average amount rates are predicated? If no, provide a detailed explanation.

b. Over the forecasted period will the over- and under-collections balance out? If no, provide a detailed explanation.

15. Refer to Thomas C. DeWard's Direct Testimony, page 16, G - Overstatement of Rate Base Due to Excessive AFUDC Accruals. Explain how this proposed adjustment differs from the AFUDC adjustment the AG/LFUCG proposed in Case No. 10481.[1]

16. Refer to Thomas C. DeWard's Direct Testimony, pages 16 and 17, H - Source of Supply - Proposed Ohio River Project:

a. The AG/LFUCG has proposed to eliminate the Ohio River Project from rate base because Kentucky-American has not obtained a Certificate of Convenience and Necessity ("Certificate"). Explain the AG/LFUCG's position regarding the other construction projects that require a Certificate that Kentucky-American included in rate base.

b. Budget project 90-13, the Kentucky River Aquatic Study, is connected to the source of supply issue and the Ohio River Project. Since the AG/LFUCG has proposed to eliminate the Ohio River Project from rate base, should this budget project also be eliminated?

17. In its May 15, 1996 response to Item 219 of the AG/LFUCG's first information request, Kentucky-American revised its requested Other Post Retirement Employee Benefits expense. Explain what, if any, affects this has on the AG/LFUCG's recommended adjustment of $209,373 to Statement of Accounting Standard No. 106 expense.

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[1] Case No. 10481, Notice of Adjustment of the Rates of Kentucky-American Water Company Effective February 2, 1989, Order dated August 22, 1989.

18. Refer to Thomas C. DeWard's Direct Testimony, page 24, 2 - Salaries and Wages. The AG/LFUCG based its adjustment on one year where the actual payroll was under the budgeted amount. Would it be more appropriate to use a historical average to use as a basis for the proposed adjustment?

19. Refer to Thomas C. DeWard's Direct Testimony, pages 25 and 26, 3 - Incentive Compensation. Is the AG/LFUCG aware of any jurisdictions where incentive compensation is not allowed? If yes, provide a list of jurisdictions and include copies of Orders that discusses the disallowance of the incentive compensation.

20. Refer to Thomas C. DeWard's Direct Testimony, pages 33 through 35, 17 - Depreciation on Toyota Main:

a. The regulation requires that a 13-month average rate base be used in a forecasted test period. Explain why the AG/LFUCG's alternative recommendation would not be a violation of the future test-period regulation.

b. Explain why the depreciation on the Toyota main should be treated differently than depreciation for other Customers Advances transferred to CIAC during the forecasted test period.

21. Refer to Thomas C. DeWard's Direct Testimony, Schedule 40, Overstatement of Federal and State income Taxes Due to the Inclusion of Excessive AFUDC in Taxable Income.

a. Explain the difference between AFUDC and the interest capitalized for taxes.

b. How does the difference between AFUDC rate-making purposes and interest capitalised for book purposes affect deferred income taxes?

Done at Frankfort, Kentucky, this 5th day of June, 1996.

PUBLIC SERVICE COMMISSION

Linda K Breathitt

For the Commission

ATTEST:

Don Mills

Executive Director