COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN ADJUSTMENT OF RATES OF	)	
DELTA NATURAL GAS COMPANY, INC.	)	CASE NO. 99-176

O R D E R

IT IS ORDERED that Delta Natural Gas Company, Inc. ("Delta") shall file the original and 12 copies of the following information with the Commission, with a copy to all parties of record, no later than August 23, 1999. Each copy of the information 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 0f 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 its legibility. When the requested information has been previously provided in this proceeding or in Case No. 99-046[1] in the requested format, reference may be made to the specific location of that information in responding to this Order. When applicable, the requested information should be provided for total company operations and jurisdictional operations, separately.

[1] Case No. 99-046, Delta Natural Gas Company, Inc. Experimental Alternative Regulation Plan.

1. In Case No. 97-066-F,[2] Delta proposed to include its voluntary contributions to The Gas Research Institute ("GRI") in its gas cost adjustment ("GCA"). The Commission denied this request.

a. What is Delta's current position regarding GRI funding?

(1) Does Delta still propose that GRI funding should be recovered through the GCA mechanism?

(2) Is Delta proposing an alternative funding method for GRI as part of its rate case? If so, give details.

b. Is Delta aware that Western Kentucky Gas Company, in Case No. 99-070[3] presently pending before the Commission, has proposed a GRI tariff rider to recover those costs through a separate mechanism?

2. Reference testimony of John B. Brown and pages 36 and 37 of the proposed tariffs.

a. Will there be any time lag in the application of the Weather Normalization Adjustment (WNA) tariff to customers bills or is it a real time adjustment mechanism that will affect customers bills for the month in which the consumption occurs?

b. Several formulas are included in the proposed tariff. Provide an example of the calculations, based on the formulas, that Delta will use to derive a customer s bill during the heating season when the WNA would be in effect.

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[2] Case No. 97-066-F, Notice of Purchased Gas Adjustment Filing of Delta Natural Gas Company, Inc.

[3] Case No. 99-070, The Application of Western Kentucky Gas Company For An Adjustment of Rates.

c. The WNA for Columbia Gas of Kentucky was initially approved by the Commission as a pilot program. Has Delta given any consideration to proposing its WNA as a pilot? If not, why not?

3. Refer to testimony of Randall J. Walker.

a. Although the cost-of-service study supports an increase in the residential customer charge, Delta has proposed to keep the charge at the current level of $8 and apply the full amount of the increase proposed for the residential class to the commodity charge. Explain the reasoning for this rate design proposal.

b. Delta has applied a limitation to the increase for the residential class equal to 1.5 times the overall percentage increase requested. Was the choice of 1.5 entirely judgmental or were there quantifiable reasons for the choice of that ratio?

(1) Could the choice of 1.5 be characterized as arbitrary?

(2) Is there any more reason for 1.5 than 1.3, 1.4 or 1.6?

c. Refer to the significant differences in class rates of return. Has any consideration been given to whether the use of one basic rate schedule, the GS schedule, for all firm customers has contributed to the magnitude of these differences? Identify the advantages of maintaining one rate schedule for all firm customers. Identify any reasons why Delta would be opposed to establishing separate rate schedules for the different classes of customers presently served under the GS rate schedule.

4. The testimony of Robert C. Hazelrigg refers to having a difference of $.25 per Mcf between firm and interruptible rates in the proposed rates and that this was the difference prior to Delta s last rate case, Case No. 97-066. Are there specific reasons

for reverting to the $.25 difference? Why not $.20 or $.30 difference? Provide complete cost justification for the amount selected.

5. Refer to Delta s response to the Commission's data request dated July 15, 1999, Item 8, page 1 of 4. For the 12 months ended December 31, 1998, define the source of $527,243 shown as other income. If this is income from special charges, show in detail the income resulting from each charge.

6. Provide exhibits to the direct testimony of William Steven Seelye on electronic media, i.e., diskette, for the adjusted test year at current rates and proposed rates. In addition, if subsequent scenarios are filed, provide electronic versions.

7. Provide a reconciliation of your cost-of-service study and the testimony of John Hall.

8. Provide a reconciliation of the results of the cost-of-service study and the rate design prescribed by Randall J. Walker. Describe both similarities and variances.

9. a. Is the cost-of-service model as presented the result of a standard industry model? If so, provide source material and state why the selection of this model was made.

b. What other companies use this model?

c. What concerns or modifications have other state regulatory commissions expressed about the model presented in this case?

10. a. What other models were considered prior to selecting this model?

b. Did other models reviewed provide similar results and guidance?

c. If not, why was this model superior? If no other model was reviewed, how is this Commission assured that the guidance represented by this model is the most reasonable?

d. If not, how was this model selected and what assurance is made to Delta as to its reliability?

11. It is stated that the gas supply functional group was not utilized because the gas supply costs have been removed from the test-year operating results. Explain why this procedure was taken. How does this impact the results of the cost-of-service analyses?

12. Provide a list with associated results of internally generated functional vectors in a form comparable to those explicitly determined.

a. What is the basis for the explicitly determined vectors?

b. Were any other methods considered for determining the explicit vectors?

c. If so, why were they not chosen?

d. If not, how can it be assured that the best possible explicit vectors have been selected?

13. a. How were the allocation factors used in the study chosen?

b. Were any other methods for determining allocation factors considered?

c. If so, why were they not chosen?

d. If not, how can it be assured that the best possible allocation factors have been selected?

14. a. How were the cost-weighting factors determined for the customer accounts' allocation factor?

b. Were any other methods for determining these factors considered?

c. If so, why were they not chosen?

d. If not, how can it be assured that the best possible cost-weighting factors have been selected? Explain this process of weighting customer accounts.

15. The zero intercept method has been utilized in the preparation of this study. How is it superior to the minimum system approach?

16. a. Has a minimum system approach been evaluated in this proceeding?

b. If so, how do the results differ from those of the zero intercept approach?

17. Provide a revised Exhibit 5 utilizing the returns determined in Exhibit 2. How do the results match the rates proposed in this proceeding? If there are significant variances, explain why these variances occur and provide recommendations to move the proposed rates in the direction of diminishing variances.

18. a. Based upon the results contained in Exhibit 5, what would the proposed rates of Delta need to be?

b. Are these rates feasible?

c. Why or why not?

19. Provide all revisions to the testimony, schedules, and other supporting documentation, filed in Case No. 99-046 and incorporated into this proceeding,

necessary to update Delta s experimental alternative rate mechanism to the current test year proposed in Delta s current rate proceeding.

20. Explain Delta s position regarding how any approved rate adjustment and any approved alternative rate mechanism would be implemented at the time the Commission enters its final Order in the current proceeding.

21. If the Commission were to approve an alternative rate mechanism, similar to that which Delta proposes, at some point during Delta s budget cycle, would it be Delta s intention to implement the mechanism on the date of the Order, or would Delta desire to postpone implementation of the mechanism until the beginning of a new budget cycle? Fully explain and justify your response.

22. If Delta were to implement its alternative mechanism during an ongoing budget cycle, explain how the mechanism would be adjusted to reflect the passage of part of the budget cycle upon which the mechanism is based. Provide all supporting documentation and workpapers to support your response.

23. Provide copies of the workpapers, calculations, and other documentation to support each of Delta s proposed adjustments disclosed in the middle two columns of the balance sheet included in Item 38 of the application.

24. In Item 38 of its application, Delta made several adjustments to its balance sheet to back out its subsidiaries and Canada Mountain. Provide a revised balance sheet showing these adjustments separately for the subsidiaries and Canada Mountain.

25. Refer to Item 25 of Schedule 7 of the proposed rate base.

a. Explain why Delta has not allocated any of its prepayments, materials and supplies, gas in storage, unamortized debt, or advances for construction to any of Delta s subsidiaries.

b. Provide an explanation for Delta s adjustment of $541,248 to its unamortized debt. In the explanation, include documentation to support the 85.17 percent factor.

c. Delta s proposed rate base does not include construction work in progress (CWIP) as a separate line item. Identify the amount of CWIP, if any, and the line item where it is included.

d. Provide all workpapers, calculations, and documentation necessary to support the $1,097,255 in total working capital.

26. In Delta s previous rate case, the Commission followed its historical precedent by adjusting rate base to reflect the 13-month average account balances for prepayments, materials and supplies, and gas in storage.

a. Explain why Delta used the end-of-period balances in its proposed rate base rather than the 13-month average balances.

b. Determine how the 13-month average balances for the above accounts would impact Delta s proposed rate base and revenue requirement. Include all workpapers, calculations, and assumptions used by Delta in its determination.

27. Refer to Delta s response to Item 12 of the Commission s July 15, 1999 Order.

a. Reconcile the $109,367,104 in the December 1998 balance for Account No. 101, Plant In Service, with the $114,965,626 in property, as reported in Item 25, Schedule 7, of the application.

b. Reconcile the $32,717,506 in the December 1998 balance for Account No. 10801, Depreciation Reserve, with the $35,230,946 in reserve for depreciation, as reported in Item 25, Schedule 7, of the application.

28. Refer to Item 38, Proposed Balance Sheet, of the application.

a. Reconcile the $112,470,779 in utility plant with the $114,965,626 in property, as shown in Item 25, Schedule 7, of the application.

b. Reconcile the $32,756,310 in accumulated provision for depreciation with the $35,230,946 in reserve for depreciation, as shown in Item 25, Schedule 7, of the application.

29. Refer to payroll adjustments, W/P 4-1, included in Item 25 of the application.

a. Reconcile the $5,893,686 in actual payroll with the $6,251,888, as shown in Item 25 of Schedule 6, as well as with the $6,175,661 in 1998 salaries and wages included in the response to Item 18(c) and the $5,952,002 total included in the response to Item 19, both of the Commission s July 15, 1999 Order. Include an explanation for each item included in the reconciliation.

b. Provide workpapers, calculations, and other documentation to support Delta s annualized payroll of $6,009,885. Delta s workpapers should identify each employee and position, the actual hours worked during the test period, the overtime hours worked during the test period, the wages effective prior to July 1, 1998, the wages effective July 1, 1998, and the percentage increase by employee.

30. Refer to Item 25, Schedule 4, of the application.

a. Provide detailed workpapers, calculations, and other documentation to support the following proposed adjustments.

(1)	Medical Adj.-Stop Loss	$ 77,561
(2)	New Customers Added	$ 54,498
(3)	Rate Case Cost	$145,000

b. Provide a breakdown, by account and amount, of the $121,120 adjustment to remove expenses related to the Canada Mountain project from the expenses includable for rate-making purposes.

c. Provide a breakdown, by account and amount, of the $142,711 adjustment to reflect the accounts disallowed in Case No. 97-066.

d. Has Delta included any of its proposed rate case cost of $145,000 in test-period operations and maintenance expenses?

e. On page 4 of his direct testimony, John F. Hall states that rate case expense will be amortized over 3 years; however, the amount of amortization requested on Schedule 4 appears to be based on a 5-year amortization period. Which rate case amortization period is correct?

31. Refer to WP51 included in Item 25 of the application.

a. Reconcile the $119,777,118 in utility plant as of December 31, 1997 with the $125,206,004 in utility plant per books on December 31, 1998 in Item 38 of the application.

b. Provide detailed workpapers, calculations, and other documentation used by Delta to arrive at the following depreciation adjustments.

(1)	Canada Mountain	$463,710
(2)	Transportation Equipment	$413,001
(3)	Power Operating Equipment	$119,391
(4)	Tranex	$126,144

32. Refer to Schedule 6 of Item 25 of the application.

a. Explain whether the payroll taxes totaling $480,841 represent the payroll tax on total payroll or payroll tax on only the direct payroll of $6251,888. Additionally, if the payroll tax is on total payroll, provide the payroll tax only on the direct payroll.

b. Provide detailed workpapers, calculations, or other documentation to support Delta s adjustment of $47,147 to remove Canada Mountain s property taxes.

33. Refer to Schedule 8 of Item 25 of the application.

a. Provide detailed workpapers, calculations, and other documentation to support the $973,775 in income tax book.

b. Reconcile the $973,775 in income tax per books with the $1,501,800 in book state and federal taxes, as reported on Schedule 2, included in the response to Item 21(a)(7) of the Commission s July 15, 1999 Order. Include an explanation for each item included in the reconciliation.

34. Describe the method of accounting for income taxes Delta is using for its financial statement purposes.

35. Refer to page 3 of 5 included in the response to Item 12 of the Commission s July 15, 1999 Order. Provide detailed workpapers, calculations, or other forms of documentation to support the determination of each separate component making up deferred taxes of $8,436,725.

36. Refer to Schedule 8 of Item 25 of the application. Delta s interest deduction of $3,114,019 is based on the debt levels and cost of debt as of the end of the test period; however, Delta has proposed to base its revenue requirement on rate base. Explain why Delta did not apply its weighted cost of debt to its rate base, as the Commission did in Case No. 97-066.

37. Refer to Schedule 9 of Item 25 of the application.

a. Provide a breakdown of the $13,580,916 adjustment to exclude Canada Mountain from Delta s capital structure. Reconcile the capital allocated to Deltran, Inc. (Deltran) as identified in this breakdown with the rate base as calculated by Deltran in its most recently approved gas cost recovery filing.

b. Provide a breakdown, by subsidiary, of the $1,280,279 adjustment to exclude the subsidiaries from Delta s capital structure.

38. Refer to the response to Item 26(a) of the Commission s July 15, 1999 Order. Provide an analysis of the test-period billings for professional services to reflect the charges incurred for matters involving Delta s subsidiaries. Reconcile these charges to the proposed adjustment included in Item 25 of the application. For any sub-account for which an allocation was not reflected, provide a detailed explanation for not removing the entire amount from the operating expenses for rate-making purposes.

39. Refer to the response to Item 28 of the Commission s July 15, 1999 Order.

Provide all workpapers, calculations, and other documentation necessary to support the amount of its lobbyists salaries Delta proposes to exclude from the test period.

40. Refer to the response to Item 29 of the Commission s July 15, 1999 Order.

a. Reconcile the balances in each of the accounts shown for the test period with the adjustments reflected in the balance sheet provided in Item 38 of the application.

b. Provide a detailed explanation for the changes in the following accounts:

(1) Net Plant Investment.

(2) Receivables from Others.

(3) Receivable from Parent.

(4) Taxes Payable.

(5) Revenues from Parent.

(6) Gas Costs.

(7) Expenses -- Other.

41. Refer to the response to Item 40 of the Commission s July 15, 1999 Order. Provide a breakdown of the Other Compensation column for 1998. This breakdown should include a description of the other compensation, the amounts, and the business reason for the compensation paid.

42. Refer to the response to Item 36 of the Commission s July 15, 1999 Order. Explain the reason Delta has not capitalized interest on construction.

43. Provide a detailed description, including all workpapers, calculations, and other necessary documentation, such as a cost allocation manual, of the allocation

methodologies used by Delta when making allocations (direct or indirect) to and from affiliated companies. Additionally, provide the total amount of these allocations, by account and subsidiary, for the test period and the 2 years preceding the test period.

44. Refer to page 19 of the 1998 Annual Report provided in Item 34 of the application.

a. Delta provides a non-contributory pension plan that covers all of its eligible employees. During the test period, did Delta make any contributions to the employee pension plan?

b. Provide a copy of Delta s most recent actuarial report concerning its employee pension plan.

c. Delta reported an accrued pension asset of $852,883 as of June 31, 1998. Provide Delta s December 31, 1998 accrued pension asset balance.

d. Provide a detailed explanation of why Delta did not propose to reduce its rate base by the balance in its accrued pension asset.

45. Provide a comparison of Delta s 1997, 1998, and 1999 employee health insurance premiums. The comparison should include the type of coverage provided, the total premium per employee, the amount of premium paid by the employee, the amount of the premium paid by Delta, and the percentage increase over the previous year s premium. Identify any measures Delta has implemented to control the rising health care insurance costs.

46. What impact would approval of the WNA tariff have on variability of revenue collections?

a. On earned return on equity?

b. On the cost of equity?

47. Refer to the response to Item 18 of the Commission s July 15, 1999 Order. Provide a detailed explanation for the variances in the following accounts. Also give a detailed analysis of any extraordinary charges included in the test-period totals.

a. 1856000 Right of Way Clearing

b. 1880050 Uniforms

c. 1881020 Rent Land & Land Rights

d. 1900020 Opr Transportation Expenses

e. 1903020 Customer Collections & Records

f. 1904000 Uncollectible Accounts

g. 1928000 Regulatory Commission Expense

h. 1930020 Company Memberships

i. 1930080 Stockholder Reports

j. 1921060 Miscellaneous Other Items

k. 1923010 Outside Services Legal

l. 1923040 Outside Services Other

m. 1408020 Property Taxes

48. What impact does Delta s policy of providing 200 feet free on new extensions have on Delta s earned return on equity?

49. Refer to lines 11-15 of page 11 of Martin J. Blake s direct testimony. This indicates that Delta s payout history has had an adverse impact on Delta s ability to earn its allowed rate of return. Who sets Delta s payout ratio? What steps could be taken to adjust the payout ratio so that the return would not be negatively impacted?

50. Refer to Delta s response to Item 2 of the Commission s July 15, 1999 Order. During the 10-year period from 1988-1998, 1988 is the only year that Delta did not earn below the imputed 43.5 percent capital structure equity component proposed by Martin J. Blake. Explain why such a common equity component is reasonable in light of the fact that the test year common equity component is shown to be 31 percent.

51. Is Martin J. Blake s proposed leverage premium premised on the reasonableness of his proposed imputed capital structure?

52. Is Martin J. Blake aware of any state regulatory commissions applying a size premium or a leverage premium in determining the appropriate cost of equity for a regulated LDC?

53. Provide copies of the Hilliard Lyons, Edward Jones, and Ibbotson reports that are referenced in Exhibit MJB-4 of Martin J. Blake s direct testimony.

54. Provide the calculations that produce the rates of return set out on page 3 of Exhibit MJB-4 of Martin J. Blake s direct testimony.

55. Refer to the direct testimony of Martin J. Blake. Did Mr. Blake consider the impact of the alternative rate mechanism, as proposed by Delta, on Delta s required return on equity? Fully explain your response.

56. With regard to Delta s proposal to use a hypothetical capital structure,

a. Discuss the appropriateness of using a hypothetical capital structure when establishing a utility s revenue requirements when the utility is also proposing to implement an alternative rate mechanism that includes an incentive based on the utility s earned return on common equity.

b. Does Delta intend to modify its alternative rate mechanism to reflect the use of a hypothetical capital structure in establishing the utility s revenue requirements?

c. Explain how establishing rates, based on the hypothetical capital structure proposed by Delta, will impact the return on actual common equity and hence the functioning of the alternative rate mechanism proposed by Delta.

57. Refer to the response to Item 2 of the Commission s July 15, 1999 Order.

a. Provide Delta s average capital structure for the 10-year period of 1988 through 1998. Include all workpapers, calculations, and other forms of documentation used to perform the calculation.

b. Delta s common equity declined from 46.7 percent of total capital in 1988 to 40.8 percent in 1999. Provide a detailed explanation for the 5.9 percent decrease in the ratio of equity to total capital.

c. For the 10-year period between 1988 and 1998, Delta s equity has exceeded 40 percent of total capital only twice; however, on page 16 of his direct testimony, Martin J. Blake, recommends an imputed capital structure of 43.5 percent common equity and 56.5 percent debt. Given the historic trend in Delta s capital structure, how realistic is it to expect that Delta will achieve its imputed capital structure?

58. How does Delta intend to achieve its imputed capital structure of 43.5 percent common equity and 56.5 percent debt?

59. Refer to the February 1, 1999 letter provided in the response to Item 39 of the Commission's July 2, 1999 Order in Case No. 99-046. Provide copies of the following budget account worksheets referenced in Delta's letter:

a. Budgeted and actual amounts by month for fiscal year 1998.

b. Budget and actual amounts by month for calendar year 1998.

c. Budget amounts by month for fiscal year 1999.

60. Provide Delta s budgeted capital structure for 1999 and for 2000 when available.

61. Describe the impact Delta s imputed capital structure will have on its cost of debt.

62. Explain why Delta did not propose to adjust its cost of debt to reflect its imputed capital structure.

63. Refer to John Hall s direct testimony, Other Proposed Tariff Changes," Exhibit 1, page 2 of 2, lines 24-26.

a. Define the term gross negligence as used in Customer s Liability.

b. Explain why Delta wants to change its duty toward its customers.

64. Provide an analysis of the costs Delta has incurred to prepare its systems for the year 2000. This analysis should include a description of the service performed, stating whether the cost was expensed or capitalized, and the year the cost was incurred.

Done at Frankfort, Kentucky, this 11th day of August, 1999.

By the Commission

ATTEST:

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Executive Director