

**KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2004-00103
FORECASTED TEST PERIOD FILING REQUIREMENTS
EXHIBIT NO. 35**

Description of Filing Requirement:

Affiliate, General or Home Office Allocations

Response:

Please see attached.

For electronic version, refer to KAW_APP_EX35_043004.pdf

**KENTUCKY-AMERICAN WATER
CASE NO. 2004-00103
FORECASTED TEST PERIOD FILING REQUIREMENTS
AFFILIATE, GENERAL OR HOME OFFICE ALLOCATIONS**

Kentucky-American Water Company (KAWC) has amounts charged and allocated to it by American Water Works Service Company, Inc. (Service Company) and American Water Resources, Inc. DVA American Carbon Services.

American Water Works Service Company, Inc.

	Amounts Allocated Charged to KAWC (000)
2001	\$2,300
2002	3,186
2003	3,286
Base Period	3,028
Forecasted Period	3,800

A contract between KAWC and the Service Company provides detailed language outlining the methodologies utilized in the allocation of Service Company charges to Kentucky-American Water. The contract became effective October 1, 1989.

The methods used to allocate charges to KAWC during the base period and the forecasted test period was based on this Service Company contract. Service Company costs are allocated to KAWC based upon actual time charged or allocated by Service Company employees as reflected in their daily timesheets. All costs of Service Company employees that are identified as related exclusively to KAWC are charged directly to KAWC. Service Company costs incurred in rendering services to KAWC, and other operating companies, are allocated among the group of companies receiving the service rendered. The allocation of these costs is based on the number of customers served at the immediate preceding calendar year end. Appropriate overhead costs actually incurred by the Service Company are added to the employee costs. Overhead costs include support personnel (secretary, mailroom clerk, telephone operator, etc.), employee benefits (group insurance, pensions, payroll taxes, etc.), building costs (rent, depreciation, maintenance, etc.), and other items (stationary, postage, legal fees, etc.). These overhead costs are assigned to each of the affiliated companies based on the labor cost dollars that were either directly billed or allocated using the formula allocation.

American Water Resources, Inc. DVA American Carbon Services

	Amounts Charged To KAWC
2001	\$ 82,000
2002	87,000
2003	91,000
Base Period	94,000
Forecasted Period	100,000

KAWC also has a lease agreement with American Water Resources, Inc. DVA American Carbon Services (ACS). This agreement is for the leasing of Granular Activated Carbon (GAC). The pricing of this agreement was based on the Company receiving competitive bids from ACS and two other companies. ACS's bid produced the best cost to Kentucky-American Water. Forecasted test period and base period amounts were calculated based upon current contracts and anticipated contracts for GAC.

Service Company Charges in Rate Filings

The Service Company charges to the various regulated subsidiaries for the services rendered reflect the contractual arrangement in the current Service Company Agreement. However, even in those jurisdictions which must approve the Service Company Agreement (i.e., because it is an "affiliate arrangement"), the regulatory commissions still assert that they have the right to approve the amount and nature of those charges in rate filings. As a consequence, as the regulated company prepares its rate filing, Rate Department personnel review the statements and supporting information for the Service Company activities charged to the Company. This contractual agreement is also subject to review by the outside auditors. During the course of these pre-filing reviews, any improper charge or allocation is adjusted prior to the filing of the case. Thereafter, these charges are also reviewed by the regulatory staffs during their audits or reviews of the reasonableness of those charges. The first contract, labeled "1971 Agreement" was in force until September 30, 1989. The second contract, labeled "1989 Agreement" became effective October 1, 1989. Both contracts provide detailed language outlining the methodologies utilized in the allocation of Service Company charges to Kentucky-American Water.

The methods used to allocate charges to KAWC during the base period and the forecasted test period will be based on the 1989 Service Company contract.

Annual Business Plan

Each year, each office and department of the Service Company is required to develop a Business Plan for the following year. During the year, each month of the business plan versus actual performance of the various Service Company offices and departments is reviewed.

Annual business plan guidelines are prepared for various areas of forecasting for the future such as for labor increases, group insurance, risk insurance, office space costs, etc. These guidelines are then followed by each office and department in the preparation for the annual business plan for the following year.

All of this is done with an eye toward providing the most professional, efficient services possible for the regulated company at the lowest reasonable cost.