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BEFORE THE
COMMONWEALTH OF KENTUCKY
PUBLIC SERVICE COMMISSION

IN THE MATTER OF:

ADJUSTMENT OF THE RATES OF
KENTUCKY-AMERICAN WATER COMPANY

CASE NO. 2004-00103

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1 CHAIRMAN GOSS:

2 Good morning, everyone. Thank you for coming back.
3 Commissioner Williams is here. She's just finishing up
4 a phone call and will join us in just a minute. If you
5 all don't mind, we'll go ahead and dispose with some of
6 the preliminaries, and we'll get started with Ms.
7 Crane, and she'll be down here in just a second. Are
8 there any matters to take up before the Commission
9 prior to Ms. Crane taking the witness stand?

10 MR. WUETCHER:

11 Your Honor, just to give you an update where we stand
12 on Dr. Vander Weide's appearance before the Commission,
13 the company has spoken or had communication with Dr.
14 Vander Weide, and they've indicated that the week of
15 the 23rd of November would be a suitable week. I have
16 checked with the Commission scheduler to see if there's
17 a possibility. There does appear to be a window within
18 your schedules that week that would permit for a few
19 hours of taking testimony, and we are now in the
20 process of seeing if the feasibility of doing the video
21 conferencing will - let me rephrase that - seeing if
22 the video conferencing method is feasible.

23 CHAIRMAN GOSS:

24 Okay.
25

1 MR. WUETCHER:

2 We won't know that until the Information Technology
3 personnel here at the Commission have made contact with
4 the personnel at North Carolina. So we don't expect to
5 have any final word for the Commission until probably
6 sometime next week.

7 CHAIRMAN GOSS:

8 All right, but you have checked with our three
9 scheduling ladies and . . .

10 MR. WUETCHER:

11 At this point in time, I spoke with Ms. Dotson and she
12 said that, based on her review of your all's schedule,
13 there appears to be a window of opportunity . . .

14 CHAIRMAN GOSS:

15 A window of opportunity, the old window of opportunity.

16 MR. WUETCHER:

17 . . . on Tuesday, November 24.

18 CHAIRMAN GOSS:

19 Okay.

20 MR. WUETCHER:

21 I believe you all have a hearing scheduled earlier that
22 day, but, at this point, I think the Commission Staff
23 persons working the case did not anticipate it going
24 much longer than the morning time period.

25

1 MR. INGRAM:
2 That is Tuesday, the 23rd.
3 CHAIRMAN GOSS:
4 Tuesday, the 23rd, yeah.
5 MR. WUETCHER:
6 Tuesday, the 23rd. I'm sorry.
7 MR. INGRAM:
8 That's all right.
9 CHAIRMAN GOSS:
10 Yeah.
11 MR. WUETCHER:
12 I'm getting my dates mixed up again.
13 CHAIRMAN GOSS:
14 Okay. Mr. Ingram?
15 MR. INGRAM:
16 Sir?
17 CHAIRMAN GOSS:
18 Is that suitable?
19 MR. INGRAM:
20 Absolutely, yes.
21 CHAIRMAN GOSS:
22 Okay, and, Mr. Spenard?
23 MR. SPENARD:
24 Yes, sir, we will hold that open.
25

1 CHAIRMAN GOSS:

2 Okay. Thank you. Okay. Well, let's shoot for that,
3 then. I guess, in terms of the length of the hearing
4 and in terms of getting Dr. Vander Weide taken on the
5 23rd, is that going to require us to alter the briefing
6 schedule probably?

7 MR. WUETCHER:

8 Your Honor, I was . . .

9 CHAIRMAN GOSS:

10 We can address that at the end of the hearing, but
11 let's talk about it just a second now.

12 MR. WUETCHER:

13 I was speaking with the Court Reporter a little earlier
14 this morning about that, and, based on the terms of the
15 contract, the requirement for when the transcript has
16 to be made available to the parties is based on the
17 last day of a hearing. So that would require - since
18 the last day of the hearing would be at the end of
19 November, November 23rd, it's probably going to extend
20 or at least reduce the amount of time that the parties
21 would have with a completed copy of the transcript
22 before they file their brief. So the parties may . . .

23 CHAIRMAN GOSS:

24 Well, I don't want to do that to them because this is a
25 fairly complex case.

1 MR. WUETCHER:

2 If that . . .

3 CHAIRMAN GOSS:

4 If we moved it to, say, the 1st of January or
5 thereabouts, would that still give us time, do you
6 think, to decide the case within the statutory period?

7 MR. WUETCHER:

8 It probably would, Your Honor. It might reduce the
9 amount of time for reply briefs to perhaps only seven
10 days. I think the Commission had already suggested
11 that the time for reply briefs would be the first
12 Friday in January. If we move that back a week and
13 allow the parties until the first Friday in January to
14 file their initial briefs, that would probably allow
15 sufficient time. Since I'm not writing a brief,
16 though, I'll let the counsel of the parties address
17 that issue.

18 MR. INGRAM:

19 Mr. Wuetcher, I have no objection if you want to write
20 a brief and file it in this matter. Your Honor, it
21 doesn't matter. Just enter a procedural schedule and
22 we'll abide by it.

23 CHAIRMAN GOSS:

24 Okay. I appreciate that. I don't want to hamstring
25 you all, though. I don't want to give you what amounts

1 to 12 days, if my math's right, for you all to prepare
2 a brief. You probably know what you're going to say
3 anyhow, but I know I've written enough of them, and I
4 like as much time as I can get even if we are talking
5 about doing them over holidays. So why don't we think
6 about - they're currently due December 20, I believe,
7 under the procedural schedule.

8 MR. INGRAM:

9 Yes.

10 CHAIRMAN GOSS:

11 If we made them due the 31st of December, that would
12 give you another 11 days. I understand the Christmas
13 holidays intervene in there, but that would give you
14 essentially half a week before Christmas and the whole
15 week before the New Year holiday. So do you all think
16 that would be okay? I'll tell you what; we could
17 just move that over to the next Monday, which would
18 be January 3. Let's just make the briefs due, then,
19 January 3.

20 MR. SPENARD:

21 Mr. Chairman, is the 3rd a holiday and will State
22 offices be open on the 3rd?

23 CHAIRMAN GOSS:

24 That's a good question, Mr. Spenard. Does anybody
25 know? The 3rd is a State holiday?

1 MR. SPENARD:
2 I believe it is.
3 CHAIRMAN GOSS:
4 Well, we'll move it to the 4th, then.
5 MR. SPENARD:
6 Yes, sir.
7 CHAIRMAN GOSS:
8 Then a week for reply briefs, that would move it to the
9 11th. So we're talking January the 11th, Mr. Wuetcher.
10 Does Staff believe they can sort through the briefs and
11 digest them and get the thing in shape for a decision
12 by the Commission? Do you know, right off the top of
13 your head, the statutory deadline date?
14 MR. WUETCHER:
15 I believe it's on or about February 28th.
16 CHAIRMAN GOSS:
17 So that gives us a month and a half.
18 MR. WUETCHER:
19 And I don't think that that changes it too much from
20 what we had originally proposed to the Commission at
21 the beginning of the hearing since reply briefs would
22 have originally been due on January 7th.
23 CHAIRMAN GOSS:
24 Okay.
25

1 MR. WUETCHER:

2 So moving it back to January the 11th is not going to
3 significantly reduce the remaining time.

4 CHAIRMAN GOSS:

5 Okay. Does that sound okay to you, gentlemen?

6 MR. SPENARD:

7 Yes, sir.

8 CHAIRMAN GOSS:

9 Okay. I don't see Mr. - well, I don't see any of the
10 Three Musketeers here today, Mr. Ockerman, Mr.
11 Barberie, and Mr. Childers. So I don't suppose they
12 have a . . .

13 MR. HOWARD:

14 I think some of those gentlemen had indicated that they
15 would be watching this one from the live stream.

16 CHAIRMAN GOSS:

17 Yeah, that's right. Well, I probably shouldn't have
18 called them the Three Musketeers, then, if they're
19 watching. If they're watching, I would have called
20 them something else.

21 MR. HOWARD:

22 It'll come back to haunt you, I'm afraid, and, sir, I
23 apologize for my tardiness.

24 CHAIRMAN GOSS:

25 Oh, that's okay, Mr. Howard. You've explained it to

1 me. I saw you this morning at the Task Force hearing.
2 I appreciate you coming in. Okay. If there's nothing
3 further, then, to take up, Ms. Crane, would you come
4 around?

5 WITNESS SWORN

6 CHAIRMAN GOSS:

7 Thank you. Mr. Spenard?

8 MR. SPENARD:

9 Yes, sir.

10 The witness, ANDREA C. CRANE, after having been
11 first duly sworn, testified as follows:

12 DIRECT EXAMINATION

13 BY MR. SPENARD:

14 Q. Good morning. Please state your name.

15 A. My name is Andrea C. Crane, C-r-a-n-e.

16 Q. And have you been retained by the Office of the
17 Attorney General in this case?

18 A. Yes, I have.

19 Q. And did you file prefiled direct testimony in August on
20 the revenue requirements of Kentucky-American Water
21 Company?

22 A. Yes.

23 Q. And, at this stage, do you have any corrections,
24 deletions, or modifications to that testimony?

25 A. No.

1 Q. Okay, and, if I asked you the same questions today that
2 are contained in your prefiled direct testimony, would
3 your answers be the same?
4 A. Yes, they would.
5 Q. Okay. With regard to some surrebuttal testimony, did
6 you file surrebuttal testimony in this case?
7 A. Yes, I did.
8 Q. And, at this stage, do you have any corrections,
9 additions, or modifications to your surrebuttal
10 testimony?
11 A. No, I don't.
12 Q. And, if I were to ask you these questions, would your
13 answers be the same today?
14 A. Yes, they would.
15 MR. SPENARD:
16 Okay, and we have the affidavit for the sur-
17 rebuttal testimony, and we'll file it with the
18 Commission at the next break.
19 CHAIRMAN GOSS:
20 All right. Very good.
21 MR. SPENARD:
22 At this stage, we tender the witness for cross
23 examination.
24 CHAIRMAN GOSS:
25 Thank you, Mr. Spenard. Mr. Ingram?

1 CROSS EXAMINATION

2 BY MR. INGRAM:

3 Q. Ms. Crane, good morning.

4 A. Good morning.

5 Q. Am I correct that this is the first opportunity you
6 have had to share your opinions with the Kentucky
7 Commission?

8 A. Yes, you're correct.

9 Q. And I further assume that, in advance of doing that,
10 you've made some preparation.

11 A. Yes, I did.

12 Q. Did that preparation include examining past Orders of
13 Kentucky-American Water Company?

14 A. Yes, it did.

15 Q. Which ones did you examine?

16 A. Well, I don't recall docket numbers, but I believe
17 there were three previous Orders that were sent to me
18 from the Attorney General.

19 Q. Is it your understanding they would be the three most
20 recent Orders?

21 A. That was my understanding; yes.

22 Q. If I gave you the numbers, would that ring a bell
23 or . . .

24 A. No, it wouldn't. I'm not very good on docket
25 numbers . . .

1 Q. Okay.

2 A. . . . so the docket numbers probably wouldn't mean
3 anything to me, . . .

4 Q. Okay.

5 A. . . . but it was my understanding the last three cases.

6 Q. In looking at the list of testimonies that you have
7 provided across the country, I notice that that list
8 begins in 1989; is that correct?

9 A. Yes.

10 Q. Immediately prior to that time, I believe you were an
11 employee of GTE Service Corporation; is that correct?

12 A. That's correct.

13 Q. As an employee of GTE Service Corporation, did you ever
14 testify in front of a public utility regulatory body
15 anywhere?

16 A. I did not.

17 Q. Is GTE Service Corporation the equivalent, as you
18 understand it, of American Water Works Service
19 Corporation?

20 A. Yes, it is. I don't think it exists anymore, but it
21 was at that point.

22 Q. Yeah. I should have used past tense. Thank you.

23 A. Right.

24 Q. Prior to that time, for five years, you were an
25 employee of Bell Atlantic various subsidiaries; is that

1 correct?

2 A. That's correct.

3 Q. Did you ever testify in any forum during the term of
4 that employment?

5 A. I did not.

6 Q. So, when you were employed on the regulatory side, you
7 never testified anywhere; is that correct?

8 A. No. I was the supporting person to the witness. So I
9 did a lot of the rate case type activities, but I was
10 not the witness myself.

11 Q. Pardon me, but that transcript won't read the way I
12 think you intended your answer, and it was because I
13 asked the question inappropriately or didn't phrase it
14 correctly. You never testified as an employee of a
15 utility; is that correct?

16 A. That is correct.

17 Q. Thank you. You have ventured the opinion in this case,
18 have you not, that forecast data makes it more
19 difficult for regulators to assess the reasonableness
20 of a utility's claim?

21 A. Yes.

22 Q. Did you ever see this Commission make that expression
23 in any of the Orders that you reviewed?

24 A. No.

25 Q. So you're presuming to say what you think they would

1 have said; right?

2 A. Well, I'm offering my opinion as an expert witness in
3 this area.

4 Q. Well, but your opinion is that regulators have more
5 difficulty in assessing the reasonableness of a
6 utility's claim with a forecasted test year; is that
7 right?

8 A. That is correct. That's my opinion.

9 Q. You've never been a regulator; have you?

10 A. I've been a Commissioner on a Water Pollution Control
11 Commission. You know, it was a very small Commission.
12 That was a regulatory position that I held. I've never
13 been a state regulator.

14 Q. You have recommended to this Commission, after your
15 review of the filing of Kentucky-American Water
16 Company, that the requested utility plant acquisition
17 adjustment for Tri-Village and Elk Lake should be
18 denied; am I correct?

19 A. Yes, you are.

20 Q. Can you tell me the differences between that request
21 made in this case and this Commission's allowance of
22 the utility plant acquisition adjustment for the
23 Boonesboro Water District in Case No. 2000-120?

24 A. Well, I wasn't involved in the prior case, so I don't
25 know all the details of that. I do know that the

1 Commission initially decided against permitting the
2 acquisition adjustment in that case, and it was only
3 after the company came back and filed a Petition for
4 Rehearing on that issue that the Commission changed its
5 mind. So obviously I don't know what kinds of
6 documentation were reviewed in that case. I do know
7 that, based on the documentation I've reviewed in this
8 case, I don't think the acquisition adjustment is
9 appropriate.

10 Q. But you don't know that there are any material
11 differences between the request made for Tri-Village
12 and Elk Lake and that made for Boonesboro, then; do
13 you?

14 A. I'm not familiar with the details of the Boonesboro
15 case. I mean, I read the Order, but I am not familiar
16 with the underlying aspects of the acquisition.

17 Q. Did you read the transcript?

18 A. The only transcript that I read, and it was quickly,
19 was Mr. Henkes' testimony, his cross examination.

20 Q. In preparation for your testimony here, did you become
21 acquainted any way with the philosophy of the General
22 Assembly of the Commonwealth of Kentucky with respect
23 to the regionalization of water facilities?

24 A. No. I have to say no. I mean, I'm generally familiar
25 with what many Legislators do in that regard, but I

1 don't have any specifics with regard to Kentucky.

2 Q. Would you accept from me that Kentucky Revised Statute
3 224A.300 says, in part, the General Assembly finds that
4 the establishment is necessary for "... encouraging
5 regionalization, consolidation, and partnerships among
6 governmental agencies and private parties, when
7 appropriate, with the goal of making potable water and
8 wastewater treatment available to all Kentuckians
9 through the maximization of financial resources and the
10 conservation of natural resources of the Commonwealth"?

11 A. Sure, and I don't think that that's unique to Kentucky.

12 Q. Not uncommon; is it?

13 A. It's not uncommon at all.

14 Q. Do you have any basis, in fact, to believe that the
15 negotiations between Kentucky-American Water Company
16 representatives and the representatives of Tri-Village
17 or Elk Lake were anything other than at arm's length?

18 A. Yes.

19 Q. What's your reason?

20 A. Well, "arm's length" generally means that two parties
21 are negotiating in such a way that each party has the
22 incentive to provide the best possible deal or to get
23 the best possible deal for itself. I believe that,
24 when one party is negotiating with the belief that they
25 will be entitled to pass on whatever costs they incur

- 1 to regulated ratepayers, that, in my view, is not an
2 arm's length transaction, because I don't believe that
3 both parties then have an incentive to get the best
4 deal possible that they can.
- 5 Q. Would you cite me to whatever it is that led you to the
6 belief that, when negotiating, Kentucky-American was
7 convinced it was going to get a utility plant
8 acquisition adjustment if it paid more than historical
9 value for the assets?
- 10 A. Well, I think most utilities believe that regulators
11 will ultimately provide for an acquisition adjustment
12 and apparently you had, in fact, received one in the
13 Boonesboro case.
- 14 Q. So the answer to my question is there's no specific
15 fact that you've relied upon to reach that conclusion?
- 16 A. No. It's just my experience dealing with regulated
17 utilities as well as experience in the outside world
18 with regard to negotiations and what incentives you
19 have going into a negotiation.
- 20 Q. Do you have any reason to believe that the ratepayers'
21 costs for consumption of water provided by Tri-Village
22 is not less now that Kentucky-American owns the assets
23 than it would have been if Tri-Village had continued in
24 business?
- 25 A. Is not less? Does that mean it's more? Is that your

1 question?

2 Q. No. I'll try to rephrase it.

3 A. Okay.

4 Q. I'm sorry. Do you have any reason to believe that the
5 rates proposed for the Tri-Village consumers in this
6 case are any greater than they would have been if Tri-
7 Village had continued in business?

8 A. Well, there is some suggestion of that. I mean, I
9 think, as we discussed on cross examination of other
10 witnesses, generally speaking, if you have a
11 municipality, you don't have a cost of equity.
12 Municipalities generally are regulated on a debt
13 service basis. Debt tends to be cheaper, especially
14 for a municipality, than does equity. So, number one,
15 you now are adding an equity component to your
16 analysis. Also, as a private entity, you are now
17 paying federal and state income taxes, which generally
18 municipalities don't, and municipal utilities generally
19 don't pay state and federal income taxes. So that's
20 another component of the regulated revenue requirement
21 that you very often don't have in a municipal system,
22 and, finally, with regard to property taxes, you may
23 not have to pay property taxes if it's municipal
24 property. So I have not done an actual analysis of
25 that, but there's certainly a suggestion that there are

1 components of the revenue requirement now that there
2 would not have been in a stand-alone system.

3 Q. Have you become familiar with the Trihalomethane
4 problem that Tri-Village had?

5 A. I've certainly read the articles that have been
6 provided and the testimony that's been provided in that
7 regard; yes.

8 Q. Do you have any understanding of the difficulty of
9 remedying a Trihalomethane problem in potable water?

10 A. I'm sure it's a difficult process. You may have
11 noticed that I have an undergraduate degree in
12 chemistry and actually worked as a chemist for a year
13 and a half. So I probably should have even a better
14 understanding than I do, but that was a long time ago.
15 I don't doubt that it's a difficult problem to solve.

16 Q. Do you understand that Tri-Village Water District was
17 unable to solve the problem without the assistance of
18 Kentucky-American's folks?

19 A. Well, I understand that Kentucky-American came in and
20 assisted Tri-Village. I don't know that I would go so
21 far as to say that I know for a fact that they were
22 unable to solve their problem without the assistance of
23 Kentucky-American.

24 Q. They hadn't solved it, had they, Ms. Crane?

25 A. Apparently not, at the time that you came in. I don't

1 know, as I stated, why they didn't solve it, you know.
2 I don't know. I can't imagine that there wasn't some
3 way that they could have solved it themselves, but they
4 didn't. I would agree with you that they didn't before
5 you came in.

6 Q. Do you agree with me that it is advantageous for
7 Kentucky-American Central Division customers to spread
8 Kentucky-American's costs over a larger group of
9 customers?

10 A. As a general matter, I would say, yes, that's a
11 benefit.

12 Q. Do you agree with me that Kentucky-American Water
13 Company has brought economic opportunities to Tri-
14 Village and Elk Lake that did not heretofore exist for
15 those entities?

16 A. I'm not sure what you mean by "economic opportunities."

17 Q. Well, let's take the national purchasing system of
18 American Water Works, for example. Do you know
19 anything about it?

20 A. I know a little bit about it and, if, by "economic
21 opportunities," you were talking about economies of
22 scale, then I understand your question. I wasn't sure
23 what you meant, as I stated, by "economic oppor-
24 tunities," whether you were talking about opportunities
25 for the residents, or what. Are you talking about

- 1 economies of scale that are involved?
- 2 Q. Do you agree with me that the purchasing system that
3 American Water Works has is a significant advantage to
4 the consumers of Tri-Village and Elk Lake?
- 5 A. I don't know the answer to that. I would hope that it
6 would be. I would hope that it would result in lower
7 costs. Certainly, as a general rule, economies of
8 scale do provide a benefit. I don't know for a fact
9 that this particular system does. It may be, in fact,
10 that your purchasing system is so complex, given the
11 size of the American Water system, that, in fact, they
12 are getting aspects of the procurement activities that
13 they wouldn't even need if they were a stand-alone
14 system. So that's also a possibility. So I can't say
15 for sure whether or not it's a benefit or not
16 specifically to the Tri-Village system.
- 17 Q. Do you agree with me that the ownership of Kentucky-
18 American has improved the quality of water for Elk Lake
19 customers?
- 20 A. Yes, I would. I would agree with you that the quality
21 has improved. Again, I guess there's a question of
22 whether or not that could have been done by Elk Lake on
23 its own, but I would agree with you that it has
24 improved.
- 25 Q. Do you agree with me that, at the time Kentucky-

- 1 American acquired Elk Lake, there were customers who
2 had such low pressure that they were not billed for
3 water service and Kentucky-American corrected that
4 deficiency?
- 5 A. I don't know that for a fact, but I certainly would
6 accept that, subject to check, if you tell me that
7 that's the case.
- 8 Q. Do you agree with me that the purchase price of the Elk
9 Lake and the Tri-Village assets has been appropriately
10 allocated to utility and non-utility property by
11 Kentucky-American?
- 12 A. I guess I'm not sure exactly what you mean. Do you
13 mean do I think the dollar figure of the acquisition
14 adjustment is the correct number?
- 15 Q. Did Kentucky-American Water Company buy any non-utility
16 property from Tri-Village or Elk Lake?
- 17 A. I don't recall. I would say, though, that I'm not
18 challenging - in my testimony, I certainly didn't
19 challenge the quantification of the acquisition
20 adjustment, although certainly there are components of
21 the acquisition adjustment that I don't think are
22 appropriate to include should the Commission decide
23 that it was, in fact, going to approve an acquisition
24 adjustment.
- 25 Q. Do you agree with me that your recommendation for the

1 treatment of construction work in progress for
2 Kentucky-American Water Company, in this case, is
3 unprecedented by any regulatory decision of this
4 Commission?

5 A. I don't know that. I do know that, in the last few
6 Kentucky-American cases, CWIP has been included in rate
7 base. I haven't done a comprehensive search of all of
8 the Orders of this Commission.

9 Q. Ms. Crane, if you or the entity that hired you
10 subsequently discovers a regulatory opinion of this
11 case that supports your recommendation for the
12 elimination of CWIP from rate base, would you share
13 that with me?

14 A. You mean a past decision by this Commission?

15 Q. Sure. Yes, ma'am.

16 A. I'm sure my attorney will share that with you in his
17 brief.

18 Q. You are familiar, are you not, with the manner in which
19 Kentucky-American finances construction?

20 A. I'm certainly familiar, in general, with the manner in
21 which utilities finance construction.

22 Q. I don't know whether or not Kentucky-American would be
23 any different, but do you understand that Kentucky-
24 American finances construction through short-term debt,
25 which, after some period of time with appropriate

- 1 considerations for the costs thereof, is converted to
2 long-term debt?
- 3 A. That's the general practice. In addition, short-term
4 debt can also be used for other things other than
5 financing rate base, but I would certainly agree with
6 you that the practice is to use short-term debt for
7 some period of time and then roll that over into long-
8 term debt.
- 9 Q. Do you understand that there is over \$6 million
10 difference between Kentucky-American's short-term debt
11 as of August 30, 2004 and the end of the forecasted
12 test year?
- 13 A. No, I didn't look at the amount of short-term debt.
14 That would have been something reviewed by Dr.
15 Woolridge.
- 16 Q. Do you understand that the vast majority of that short-
17 term debt is going to be used to finance the
18 construction work in progress during the forecasted
19 test year?
- 20 A. Well, as I think I indicated, that wouldn't surprise
21 me, although there are certainly other components of
22 rate base that are frequently financed with short-term
23 debt.
- 24 Q. Well, if no other components of rate base financed with
25 short-term debt, is that what you said?

- 1 A. No. I said there are frequently other components of
2 rate base that are financed with short-term debt. In
3 addition to that, financing is really fungible. So, in
4 essence, it's difficult to say what component of
5 financing is actually financing what component of rate
6 base. I have agreed with you, though, that the general
7 practice is to issue long-term debt in steps and to
8 acquire short-term debt in the interim.
- 9 Q. Do you have any basis to disagree with me that the
10 \$5,980,000 of construction work in progress for
11 Kentucky-American in this forecasted test year is going
12 to be financed with short-term debt?
- 13 A. Well, I think I just indicated financing is fungible.
14 I don't know that you can actually follow a dollar of
15 financing into a dollar of rate base. I would agree
16 with you, as I've stated repeatedly, that it is a
17 general practice for utilities to take on additional
18 short-term debt and then to roll it over into long-term
19 debt.
- 20 Q. Believe it or not, I've heard you say that. If
21 Kentucky-American finances its CWIP with short-term
22 debt and CWIP is not allowed or not done, then it will
23 have no need to increase its short-term debt for that
24 limited purpose, would it, Ms. Crane?
- 25 A. Well, for that purpose, it wouldn't, but there . . .

1 Q. Okay.

2 A. . . . may be other purposes that it would, in fact, use
3 its short-term debt for.

4 Q. The elimination of any short-term debt from the
5 capitalization in the forecasted test year would simply
6 have the effect of driving up the overall cost of
7 capital; would it not?

8 A. No. It would have the effect of actually regulating,
9 in my view, along appropriate regulatory principles.

10 Q. Do you . . .

11 A. The net effect is that generally short-term debt is
12 lower cost than long-term debt.

13 Q. Sure.

14 A. So, if the Commission were to reduce the amount of
15 short-term debt in the capital structure, probably the
16 result would be a higher overall cost of capital,
17 but . . .

18 Q. Thank you.

19 A. . . . that's not, you know, why they should make
20 certain decisions.

21 Q. But that's the result of the decision, to eliminate
22 CWIP from the rate base; is it not?

23 A. Well, the result of a decision to eliminate CWIP from
24 rate base is to prevent ratepayers from paying a return
25 on plant that is not yet providing them with any

1 utility service, which may never provide them with any
2 utility service, and it also prevents them from bearing
3 the risk during project construction, a risk that, in
4 my view, should be borne by shareholders and not
5 ratepayers. So there are many results from eliminating
6 CWIP from rate base.

7 Q. In your opinion?

8 A. That's all I'm here to give, is my opinion.

9 Q. Sure. You have recommended to this Commission that
10 depreciation be eliminated as a component of a lead-lag
11 study; have you not?

12 A. Yes, I have.

13 Q. Did the Attorney General make available to you, either
14 initially or after the rebuttal testimony of Kentucky-
15 American was filed, this Commission's decision in Case
16 No. 92-452?

17 A. Well, as I've indicated, I admit I'm pretty bad on
18 docket numbers. However, that sounds like an old one.
19 I don't know whether they did or not.

20 Q. Okay.

21 A. You'll have to tell me what that case is and then . . .

22 Q. Sure. It was an adjustment of the rates of Kentucky-
23 American Water Company wherein the issue was raised as
24 to whether or not non-cash items should be included in
25 a lead-lag study. Do you recall reading that

1 precedent?

2 A. I do recall reading about - well, I don't know. Maybe
3 that's a data request I'm thinking about. I don't know
4 whether I've seen that or not. Is that one of the last
5 three cases? If it's one of the last three, I probably
6 did see it.

7 Q. Do you recall the statement, if you read the opinion,
8 and I quote, "The record evidence persuades the
9 Commission that including net earnings and non-cash
10 items is theoretically sound," and that quote pertained
11 to a lead-lag study?

12 A. I don't remember reading that. If I had, it wouldn't
13 have changed my opinion, but I certainly don't recall
14 reading that specific sentence.

15 Q. You disagree with this Commission's previous treatment
16 of the inclusion of depreciation in a lead-lag study,
17 then, I take it.

18 A. Strenuously, I disagree; absolutely.

19 Q. You have not suggested, have you, that the amount of
20 money that Kentucky-American Water Company spent on
21 security from 9-11-01 to 4-30-04 was inappropriately
22 spent?

23 A. I have not stated that it was inappropriately spent nor
24 did I do perhaps as extensive a review of those dollars
25 as I might have done if the company had filed for and

1 received deferred accounting treatment. Since the
2 company didn't do that, I didn't think recovery was
3 appropriate. I looked at those costs, but I did not
4 perhaps do the comprehensive investigation of each
5 dollar that I might have done if my recommendation on
6 recovery had been different.

7 Q. The answer is my question is no?

8 A. I believe I indicated that I did not, in my testimony,
9 raise an objection to a specific expenditure with
10 regard to security costs.

11 Q. Do you agree with me that that expenditure was to
12 protect the assets of Kentucky-American Water Company?

13 A. Yes, I do.

14 Q. And those assets exist to provide potable water to the
15 customers?

16 A. Yes, they do.

17 Q. Do you agree with me that the accounting adjustment and
18 the deferral requested for Service Center costs and
19 Customer Care costs, in this case, had deducted from
20 them the cost savings prior to the filing in this case?

21 A. I would agree that you've amortized those costs to the
22 extent there have been cost savings. I'm not sure if
23 that's your question.

24 Q. Well, I apologize. I'll try to make my question
25 clearer, then. Do you understand that Kentucky-

1 American spent some money for its Customer Care Center
2 that's going to result in some cost savings over time?

3 A. Yes.

4 Q. And do you understand that those cost savings are
5 embedded in Kentucky-American's costs in the forecasted
6 test year in this case?

7 A. Sure.

8 Q. Do you understand that, to the extent that those cost
9 savings were realized prior to the filing of this case,
10 they were offset against the deferral requested in this
11 case for Customer Care?

12 A. Yes. In terms that the amortization has already
13 started, I would agree with that.

14 Q. Now, can I just summarize and say I'll ask you the same
15 set of questions about the Service Center, and would
16 you give me the same answers?

17 A. Yes, I would.

18 Q. So Kentucky-American, then, has matched, through the
19 beginning of the Service Center and the Call Center,
20 the cost thereof against the savings; am I right?

21 A. Well, you've begun your amortization, and you've
22 amortized to the extent of your estimate with regard to
23 savings. Whether or not there has been a true match, I
24 mean, your savings estimates may or may not be
25 accurate, number one. You know, you've done the

1 amortization. You've done the accounting. I don't
2 know if I would go so far as to say there has actually
3 been, you know, a match of costs and savings.

4 Q. Temporarily, there has been a match of costs and
5 savings; has there not?

6 A. Well, there has been a match of the amortization of
7 certain costs with the company's estimate of savings
8 during that period. That's what has really been
9 matched.

10 Q. You have not disagreed with the company's estimate of
11 the savings in this case; have you?

12 A. I haven't, but, you know, that's something that is very
13 difficult to actually track and certainly it's
14 difficult to forecast. It's very difficult to track
15 too. It's almost impossible to know whether savings
16 are the result of a specific reorganization, for
17 example, of the Service Center, whether it's the result
18 of other reorganizations that have taken place and that
19 continue to take place in your company. You know, it's
20 very, very difficult to assign a particular savings to
21 a particular action of the company. So I'm not sure
22 how - I know commissions sometimes establish formulas
23 that are supposed to track that. I'm not sure that it
24 ever really is able to be tracked.

25 Q. You disagree with me that the matching principle of the

1 savings and the costs on a time basis should continue
2 through the forecasted test year in this case?

3 A. Oh, I agree, to the extent that the company incurs
4 appropriate costs for prospective recovery, those costs
5 should be matched with rate recovery, but I don't think
6 that costs that you've previously spent and have
7 deferred without a deferred accounting order are
8 appropriate to be recovered in any case. So I have to
9 say, with regard to past costs, I disagree. I don't
10 think there is an issue of matching in that regard.

11 Q. Have you suggested in your testimony that to allow
12 Kentucky-American to defer security costs and the
13 Service Center costs and the Customer Center costs
14 would be retroactive reimbursement?

15 A. Absolutely. You have no deferred accounting order, and
16 you didn't even file for a deferred accounting order
17 until December of 2003. In addition, this is an issue,
18 at least the security costs, that was certainly alive
19 and well during your merger transition case. It was a
20 cost that you had originally come in for and asked for
21 a surcharge on. You had withdrawn that. It was
22 referenced in the merger case, how you were going to
23 recover, or the fact that you weren't going to ask for
24 additional recovery of security costs until a rate
25 case. So, yeah, I would definitely say so.

1 Q. The answer is "Yes." Ms. Crane, I'm kind of interested
2 in your mathematics in coming up with a proposal
3 for residential consumption in the forecasted test
4 year . . .

5 A. Sure.

6 Q. If I understand what you did, you took Dr. Spitznagel's
7 statistically derived projection of 165.42 gallons per
8 customer per day, and you picked a number out of the
9 last rate case of 183.94 gallons per day, and you
10 averaged them for a recommendation for calculating
11 revenues of 174.68 gallons per day; am I correct?

12 A. I have to put the glasses on for this one. Yes, 174.68
13 gallons.

14 Q. Do you understand, based on the rebuttal testimony
15 that's been filed in this case, that your
16 recommendation constitutes a forecasted test year
17 consumption per residential consumer that is higher
18 than the 2003 residential consumption of Kentucky-
19 American?

20 A. Sure, and I would expect that. 2003 was the wettest
21 year in, like, the past five years. I think we had
22 some cross examination on that. So I would definitely
23 expect that prospective consumption would, in fact, be
24 higher.

25 Q. Do you agree with me that precipitation was not a

1 factor correlated to consumption by Dr. Spitznagel?
2 A. Well, I believe that Dr. Spitznagel used the Palmer
3 Severity Drought Index and actually, if you go in to
4 look at that index, that is an index, at least from
5 what I have found on my Internet search, that actually
6 looks at both rainfall and temperature. So, in my
7 understanding of the index, there is actually a
8 component of precipitation in the index, precipitation
9 and temperature, both.
10 Q. Those are not the only two factors considered in the
11 Palmer Drought Index; are they?
12 A. I don't know what else is considered, and it wouldn't
13 surprise me to know that there were other factors
14 considered.
15 Q. Such as days of sunshine?
16 A. If you are telling me that, I would accept that,
17 subject to check.
18 Q. Such as humidity?
19 A. I don't know that, but, again, if you're warranting
20 that to me, I would accept that, subject to check.
21 Q. Such as wind?
22 A. Again, I would accept that, subject to check.
23 Q. Did you make any statistical analysis to determine the
24 reasonableness of your utilization of 183.94 gallons
25 per customer per day that you picked out of the last

1 case?

2 A. No, but I did make an analysis of the reasonableness of
3 my recommendation, . . .

4 Q. Okay.

5 A. . . . which is 174.68 gallons.

6 Q. You understand, then, that, during the base period in
7 this case, the residential consumption was actually
8 less than Dr. Spitznagel projects in the forecasted
9 test year; don't you?

10 A. Yes, and I don't think that's surprising, and, again,
11 if you go in today and look at the Palmer Drought
12 Severity Index on the Internet, they have weekly
13 information, and I actually have gone in and looked at
14 it, and, if you look at the summer months, again, the
15 index is above normal. So I don't think that that's a
16 surprising result.

17 Q. You made no statistical effort to correlate Kentucky-
18 American's projected sales in the forecasted test year
19 to any events historically; did you?

20 A. Well, I would disagree with that, since I used two
21 numbers that had been derived, presumably, based on
22 some statistical model of past events, and I averaged
23 those two numbers. That's what I did. So I would have
24 to say that, yes, my average does take historical
25 events into consideration. In addition, I did a sanity

1 check, which I think is also important when you're
2 looking at statistical models.

3 Q. Do you agree . . .

4 A. So . . .

5 Q. I'm sorry.

6 A. So I would have to say that, in fact, I did take that
7 into consideration.

8 Q. You didn't do the work yourself; did you?

9 A. No. Our budget just wouldn't allow us to get involved
10 in that level of detail. So I just don't have the
11 resources or the money to undertake some of those
12 studies myself.

13 Q. Do you agree with me that the base period consumption
14 per commercial customer for Kentucky-American Water
15 Company is less than Dr. Spitznagel estimates for the
16 forecasted test year?

17 A. Yes.

18 Q. Do you agree with me that commercial customers
19 typically do not irrigate?

20 A. As a general rule, I would say that I would agree with
21 you that the variation of their usage is not as great
22 as residential customers. I would not agree that they
23 don't irrigate. Small commercial customers frequently
24 irrigate and, in fact, large commercial customers
25 frequently do as well, particularly if they have, you

1 know, landscaped office parks and that sort of thing.
2 So I wouldn't agree with that.

3 Q. Do you recall Mr. Miller testifying that Kentucky-
4 American was actively trying to hire individuals to
5 fill every vacancy which exists currently at Kentucky-
6 American?

7 A. Well, actually, I don't recall that. I do recall a
8 data request that indicated that many of those
9 vacancies were in the process of being filled, but I'm
10 thinking, for example, like Ms. Bridwell, I thought I
11 heard that there was not going to be a Kentucky-
12 American Water Company employee replacing her, for
13 example. So, while generally I believe that Mr. Miller
14 said, "We're looking to fill these vacancies," and
15 there was a data request response with regard to the
16 14 vacancies, I'm not sure I would go so far as to say
17 every single vacancy was in the process of being filled
18 or will be filled.

19 Q. Do you agree with me that Kentucky-American has not
20 included any compensation for temporary employees in
21 the forecasted test year?

22 A. I'm not sure whether they have or not.

23 Q. Okay. Do you agree with me that Kentucky-American has
24 removed 5,700 hours of overtime from the base year in
25 the forecasted test year?

1 A. Yes, I would agree with that.

2 Q. And, at an expected annual work effort of 2,000 hours,
3 that represents 2.85 people or 2.85 vacancies?

4 A. I'll accept your math.

5 Q. Thank you. Do you agree with me that Kentucky-American
6 has no expenses in the forecasted test year for
7 management overtime?

8 A. I know you have overtime expenses, and I don't know
9 what that consists of. So I don't know that, whether
10 or not it consisted of management overtime.

11 Q. Did you hear Kentucky-American witnesses state that
12 management is never paid overtime?

13 A. I do not recall hearing that. I'm sure the transcript
14 will speak for itself, but I have to say I don't recall
15 hearing that.

16 CHAIRMAN GOSS:
17 Mr. Ingram, are those folks salaried employees?

18 MR. INGRAM:
19 They are, Your Honor.

20 CHAIRMAN GOSS:
21 Okay.

22 Q. Do you recall, from looking at the information provided
23 by Mr. Miller in his Rebuttal Testimony Exhibit 7,
24 Page 3, that Louisville Gas and Electric Company, head-
25 quartered here in Kentucky, maintains an executive

1 compensation plan that covers not only its executives
2 but also its middle management professional people?
3 A. Yes.
4 Q. Do you understand, or do you believe that, from 1999 to
5 2003, Kentucky-American reduced its staff by
6 approximately 20 positions?
7 A. That's my understanding.
8 Q. Do you agree with me that the employee count is a
9 significant factor in determining OPEB costs?
10 A. It certainly is one of many significant factors. I
11 would agree with you.
12 Q. Others would be pay increases given annually?
13 A. That's one.
14 Q. Do you understand that Kentucky-American's employee
15 level from 2004 to 2005 has been stable?
16 A. I'm sorry. Could you repeat that question?
17 Q. Sure. Kentucky-American's employee level from 2004 to
18 the forecasted test year is stable?
19 A. Yes.
20 Q. Do you agree with me that medical costs have risen on
21 an annual basis for at least the last ten years?
22 A. Yes, and that's why it's interesting, if you look at
23 your OPEB costs, they have not risen on an annual basis
24 over the past ten years consistent with the increases
25 in health care.

1 Q. Do you now understand, from the rebuttal testimony
2 filed in this case, that sedimentation removal from the
3 basins and washwater tanks at the Richmond Road Station
4 is an annual event?
5 A. Well, I know that's what the company is saying now. I
6 mean, that's not what they said in the beginning. I do
7 understand that that was what was said in the most
8 recent rebuttal testimony, although, in a data request
9 response, it also indicated that the level of solids
10 that are expected to be removed in 2005 are not as
11 great as the level that were removed in 2004. So I
12 think there's a lot of conflicting information with
13 regard to solids removal.
14 Q. The answer to my question is yes?
15 A. I said it is my understanding that that's the company's
16 position at this time.
17 Q. Do you disagree with it?
18 A. Well, I'm a little concerned, and I'll tell you why. I
19 mean, we started this . . .
20 Q. Well, if I want to know that, Ms. Crane, with all due
21 respect, I'll ask you.
22 A. Okay.
23 MR. SPENARD:
24 Mr. Chairman, . . .
25

1 CHAIRMAN GOSS:

2 Let's let her finish. She's certainly entitled to
3 explain any answer and elaborate to the degree
4 that she wants to. We've certainly let Kentucky-
5 American's witnesses do that. So let's let her
6 go ahead and finish, if she wishes to say
7 something else.

8 A. My only concern is that the company filed its case
9 using an annual recovery period for these costs. It
10 then said, in a data request response, that it wasn't
11 going to do this removal annually. It then followed up
12 in a subsequent data request response and said, "Oh, we
13 are actually going to do it annually," and there was
14 some testimony during cross examination about
15 discussion with Production folks that led to that
16 conclusion. I'm wondering why the company initially
17 filed for annual recovery if, in fact, it didn't think
18 it was going to be doing this annually, and then it
19 seems to have shifted its position as it got data
20 requests asking about this annual recovery period. So,
21 you know, I guess, ultimately, it's going to be up to
22 the Commission to shift through this sometimes
23 conflicting information and make a determination that
24 it feels is reasonable, but I don't think it's at all
25 clear at this point.

1 Q. Do you believe, from the rebuttal testimony provided by
2 Ms. Bridwell, that it's going to be necessary to clean
3 the solids out of Lake Ellerslie on an annual basis?
4 A. That's what she has said, although she has also said
5 that the next year of solids removal will not be as
6 extensive as the prior year. "Kentucky-American does
7 not envision having to remove the same amount of solids
8 from the reservoir next year," to quote the data
9 request response.
10 Q. Has Kentucky-American had a rate case that you're aware
11 of where the question of security costs has been an
12 issue before this one?
13 A. A rate case?
14 Q. Yes.
15 A. I'm assuming that the merger case is not considered a
16 rate case. So, in that regard, I can't think of one.
17 Q. Has Kentucky-American had a rate case known to you
18 where the Customer Care Center costs or Shared Services
19 costs was an issue?
20 A. If I could back up a minute, you did file a tariff for
21 recovery of security costs. I don't know if you're
22 considering that a rate case, but I am aware that that
23 tariff was filed with regard to security costs. So I
24 don't if you would - if you would define that as a rate
25 case, then you have had a rate case for security costs.

1 With regard to Customer Care costs, I don't know if
2 that has ever been an issue. It's my understanding
3 that the specific claim that you've made in this case
4 has not been an issue in a prior case.

5 Q. Do you accept as true Mr. Miller's statement that,
6 annually, Kentucky-American Water Company writes a
7 check for 35 percent of its taxable income to the
8 entity that files a consolidated tax return which
9 includes Kentucky-American Water Company?

10 A. Yes. I don't think they should be, and we shouldn't be
11 paying for it, but I don't have any reason to doubt
12 that they actually write a check every year.

13 Q. And that check is accurately reflected on the income
14 statement of Kentucky-American Water Company or the
15 amount of that check; is that correct?

16 A. I presume it is. I mean, I'm not your auditor, but I
17 have no reason to doubt that it's appropriately
18 reflected on your financial statement.

19 Q. Do you likewise believe Mr. Miller when he says that
20 those subsidiaries joining in the consolidated tax
21 return who have a tax loss are provided the carry-
22 forward tax equivalent of that loss in cash by the
23 entity who files a consolidated tax return?

24 A. No. I believe that that's what's happening, but I
25 don't think that should be what's happening from a

1 ratemaking perspective. There's no reason for us to be
2 paying them for those tax losses. However, I don't
3 doubt that that's actually what you're doing.

4 Q. Do you agree with me that there is a significant
5 jurisdictional issue for a Commission in one state to
6 take a benefit attributable to a subsidiary that exists
7 exclusively in another state and giving it to the
8 customers over which it has regulatory authority?

9 A. I don't see that as a significant issue if my utility
10 in my state is ultimately impacted by that or should be
11 from a ratemaking perspective, which is exactly what's
12 happening here. I mean, you have - Kentucky-American
13 ratepayers are paying higher rates for taxes than their
14 counterparts, for example, in West Virginia and
15 Pennsylvania, because this Commission hasn't adopted a
16 consolidated income tax adjustment and those
17 Commissions have. So, as long as there's any impact on
18 Kentucky-American, I think it is appropriate to look at
19 the whole environment of what's going on at a
20 consolidated basis within the company and to determine
21 whether or not, from a ratemaking perspective, it
22 should have an impact on Kentucky ratepayers.

23 Q. Do you agree with me that, if Kentucky-American is not
24 allocated its full cost of service in a forecasted test
25 year, that it does not have a reasonable opportunity to

1 earn the rate of return that may be given?

2 A. No, and I'll tell you why, because it may not show the
3 same number on an income statement that this Commission
4 has authorized, but it's not unusual for a regulatory
5 commission to make ratemaking adjustments. The
6 regulatory commission looks at its pro forma revenue,
7 its pro forma expenses, and it develops whatever return
8 it decides is reasonable. When you take that
9 information and you put it on the books of the company,
10 there may be many differences in revenues; there may be
11 differences in expenses from what is used for a
12 ratemaking perspective. So I would agree with you that
13 any disallowance this Commission makes is going to
14 reduce the company's financial return. I agree with
15 that, but it is not going to reduce the return that
16 this Commission finds to be appropriate, because
17 they're going to use their pro forma level of revenues
18 and expenses in order to calculate their pro forma
19 level of return.

20 Q. Kentucky-American Water Company cannot reasonably earn
21 the return on equity awarded by the Commission. The
22 effect is merely the acceleration of the next rate
23 case, is it not, Ms. Crane?

24 A. I disagree with you completely, because they will be
25 earning. They will be earning. Based on the revenues

1 and expenses approved by this Commission, they will be
2 earning their authorized return, or they will have the
3 opportunity. I don't know whether they'll earn it or
4 not. They may overearn; they may underearn; they may
5 have to be back here in a year. I don't know that. No
6 one does, but it has nothing to do with the fact that a
7 consolidated income tax adjustment is or is not
8 accepted by this Commission. I mean, to give you a
9 smaller example, you know, there are things like
10 charitable contributions, for example, that may be
11 disallowed. Advertising may be disallowed. You know,
12 there's different treatment with regard to plant. So
13 there are lots of adjustments that are made by
14 regulatory commissions, and their finances, their pro
15 forma statements, will be used to determine whether or
16 not you have to come back for a rate increase or not,
17 not your financial books.

18 Q. Can you show me any consecutive 12-month period of
19 Kentucky-American Water Company, by virtue of its books
20 or the Commission's books, in the last ten years where
21 Kentucky-American Water Company has earned its
22 authorized rate of return?

23 A. Doesn't that strike you as odd? That strikes me as
24 incredibly odd, to tell you the truth, and, you know, I
25 cannot, but I looked at the information that Mr. Miller

1 provided, and he has five years of data, I believe,
2 and, during those five years - or maybe he has more, I
3 don't know, but I remember he has at least five -
4 during those years, you've never earned your return.
5 Now, he's looking at your financial return. He has not
6 made any ratemaking adjustments, as he indicated.
7 Okay? It may be that, if he had normalized revenues,
8 for example, you would be doing great, but it seems odd
9 to me that a utility, you know, consistently doesn't
10 earn its return. Perhaps the information that's being
11 provided in those financial statements does not comport
12 with the pro forma statements that were used by the
13 Commission when it came out with its recommendation.
14 So, you know, I can't show you that they have.
15 However, I don't necessarily think that would have been
16 provided with the correct documentation to make that
17 determination.

18 MR. INGRAM:

19 That's all I have, Ms. Crane. Thank you.

20 A. Thank you.

21 CHAIRMAN GOSS:

22 Thank you, Mr. Ingram. Mr. Childers, do you have
23 questions?

24 MR. CHILDERS:

25 Just one, Your Honor.

1 CHAIRMAN GOSS:

2 All right. Come on up here, if you don't care,
3 Mr. Childers, so the microphone can catch you.

4 CROSS EXAMINATION

5 BY MR. CHILDERS:

6 Q. Good morning, Ms. Crane.

7 A. Good morning.

8 Q. The low-income discount that's being proposed in this
9 proceeding is estimated to cost \$30,000. You were
10 aware of that; weren't you?

11 A. Yes, I am.

12 Q. And the overall rate increase is approximately
13 \$7.3 million; is that true?

14 A. That's correct.

15 Q. And isn't it true that the \$30,000 represents something
16 on the magnitude of a .3 of 1 percent of that revenue
17 increase?

18 A. I would accept that, subject to check.

19 MR. CHILDERS:

20 That's all. Thank you.

21 CHAIRMAN GOSS:

22 Thank you, Mr. Childers. Mr. Ockerman nor Mr.
23 Barberie are here. They indicated they had to be
24 in motion hour in Fayette County, I think, this
25 morning. So we know where they are, but, if

- 1 Q. Okay. Of that 175, were most of them rate adjustment
2 proceedings?
- 3 A. Yes, they were, the majority.
- 4 Q. Of those cases, how many of those involved future test
5 periods?
- 6 A. I think the only jurisdiction that I have testified in
7 that would involve a future test period as that is
8 being used here would - well, actually, my Rhode Island
9 cases, I don't know how many there are, if you went
10 through my Appendix A, my testimonies in Rhode Island,
11 they actually use a historic base year that's known at
12 the time of their filing, but then they use a forecast
13 test period that is entirely in the future. So it's a
14 little bit different from the situation here, but there
15 is a forecast test period that is 12 months in the
16 future in Rhode Island. Maybe there's a dozen cases in
17 Rhode Island that I've testified in.
- 18 Q. Okay. Well, based upon your experience, do you find
19 any difference in the quality of data or level of
20 complexity in those proceedings where a future test
21 period is used as opposed to those in which a
22 historical test period is used?
- 23 A. Absolutely.
- 24 Q. Can you tell us what that difference is?
- 25 A. Well, the biggest difference is that, when you're

1 dealing with totally forecast data, you're generally
2 relying upon a budget. Unfortunately, we all know that
3 budgets are put together for many different reasons. I
4 did hear the company indicate that they scrubbed their
5 budget, I think was the word that was used, in order to
6 try and make it as close to reality as possible.
7 However, any time you deal with budgeted data that is
8 not linked to historic data, in my view, there's a real
9 problem, because you pretty much have to take the
10 company - I mean, if they say they're going to spend
11 \$200,000, you then have to say, "Well, how do I know
12 you're going to spend \$200,000? Can you show me
13 contracts?" You know, "Have you entered into
14 arrangements?" It's very difficult to analyze whether
15 or not an increase or a decrease prospectively is going
16 to occur when your forecast test period is not linked
17 to historic data, because it's just a budget, and it
18 can bear no relationship to what actually happened in
19 the past, and that's very difficult.

20 Q. In your opinion, does the use of a future test period
21 increase the level of rate case expense?

22 A. Absolutely, and, you know, obviously to the extent
23 you're using more historic data rather than less, your
24 rate case expenses are going to go down. For example,
25 I testify in one jurisdiction that uses an entirely

1 historic rate base; no known and measurable changes.
2 Whatever the rate base was six months ago, that's what
3 they get. Well, those cases are easy. I don't have to
4 spend a dollar on analyzing their rate base. So it's a
5 whole spectrum of different methodologies that are used
6 and, as you get further away from historic data, the
7 complexity increases and the rate case costs increase
8 and the resources that have to spent analyzing the rate
9 case increase.

10 Q. So I take it, from your last answer that, in cases
11 using a future test period, there's increased discovery
12 as opposed to those using a future test period?

13 A. I'm sorry. Could you ask that question again?

14 Q. Well, let me rephrase it. I take it from your
15 statement, would it be - would you agree that it has
16 been your experience, in cases in which a future test
17 period has been used to base proposed rates, there is a
18 greater amount of discovery conducted by the parties
19 than would be in proceedings in which the proposed
20 rates are based on a historical test period?

21 A. Yes, I would agree with that.

22 Q. There was some questioning yesterday regarding the
23 benefits of a future test period, . . .

24 A. Yes.

25 Q. . . . and I believe - well, Mr. Miller discussed that

1 at length with Commission Staff. Can you tell us, in
2 your opinion, what are the benefits to consumers of the
3 use of a future test period?

4 A. I don't think there are any benefits to consumers.

5 Q. What are the benefits to the utilities of using a
6 future test period?

7 A. Well, one benefit is they get more of their - they get
8 their future plant additions recognized in rate base,
9 so they get future expenditures recognized in rate
10 base. To the extent CWIP is also included in rate
11 base, they get sort of future, future plant recognized
12 in rate base. They also - I think it has a subtle
13 shift almost in the burden of proof, because now - and
14 I'm not talking about this from a legal aspect at all -
15 I'm not an attorney - but the company now comes forward
16 and says, "This is what I'm going to spend next year,"
17 and it doesn't have to relate necessarily to historic
18 expenditures. You almost have to take them on faith
19 that this is, in fact, what they're going to spend,
20 and, in fact, another difficulty is, you know, even if
21 the company puts forth its best effort, there are
22 always events that are unforeseeable. We never know
23 whether expenditures will actually, you know, comport
24 with what has been anticipated. So the company gets to
25 develop its case without having any obligation at all

1 to tie it in, you know, directly to a historic
2 expenditure level, and so they get, you know, sort of
3 accelerated recognition of plant. They get, in my
4 view, a reduction in the amount of documentation,
5 almost, that has to be provided with regard to the
6 expense side of the equation, and I think they're two
7 tremendous benefits.

8 Q. Would you agree with the statement that, to the extent
9 that a utility would obtain significant benefits from
10 filing a future test year period, that differences in
11 the cost between the filing of a future test year
12 period and a historical test year period might
13 appropriately or should appropriately be shared between
14 the shareholders and the utility ratepayers?

15 A. Well, there's at least one jurisdiction that believes
16 that all rate case costs should be shared between
17 ratepayers and shareholders regardless of whether a
18 historic test period is used or not. So, I think, to
19 the extent there is a direct benefit to shareholders, I
20 certainly wouldn't be opposed to any proposal to have a
21 sharing of rate case costs.

22 Q. Okay. Well, let's take it a step further, then. How
23 would you measure the difference between costs for
24 filing a historical test period and filing a future
25 test period?

1 A. Well, that's very difficult. I mean, I suppose,
2 although no two cases are ever identical, you would
3 have to look at what cost level is being incurred by
4 another utility or other utilities, another group of
5 utilities, that are filing based on an historic test
6 year and try to do some sort of comparison.

7 Q. Okay. Are you aware of any jurisdiction that cur-
8 rently - you mentioned one that specifically requires a
9 sharing of costs between the shareholders and
10 ratepayers in all cases. Which jurisdiction is that?

11 A. New Jersey.

12 Q. Okay. Are you aware of any jurisdictions, aside from
13 New Jersey, that require that type of sharing of costs
14 where the company has elected a particular type of
15 filing, for example, the use of a future test period as
16 opposed to a historical cost test period?

17 A. I'm not aware of any other jurisdiction that requires
18 an explicit sharing. However, most jurisdictions use
19 some sort of an amortization with no rate base
20 treatment. That could be viewed as some sharing
21 because of the net present value implications, but it's
22 implicit rather than explicit. New Jersey is the only
23 one that I'm aware of that has the explicit sharing.

24 Q. Okay, and you're aware that Kentucky currently does not
25 allow the rate case expense - while it permits the

1 amortization of rate case expense, it does not allow it
2 in rate base?

3 A. Correct.

4 Q. At Page 8 of your testimony, you make reference to some
5 of the material that the company has filed, and you
6 refer to it as confusing, conflicting, and poorly
7 organized. Is that . . .

8 A. I did say that.

9 Q. Am I misrepresenting your description of the filing?

10 A. I did use those words; yes. You're correct.

11 Q. Based on your experience, how does the company's filing
12 compare to filings made in other states?

13 A. Well, you know, it's a real negative if you're not
14 given enough information to analyze a filing. In my
15 view, it's almost worse if you're given too much
16 information. In the company's filing, I mean, this is
17 one of my concerns, you know. For example, we talked
18 about the Service Company bills in an Excel file with
19 20,000 cells, I think, was the number that was
20 discussed during these hearings. Well, you know, when
21 you're sitting there with a spreadsheet with 20,000
22 cells, you know, it's a little bit difficult to get
23 behind the numbers and figure out exactly what's going
24 on. Similarly, when you look at what the company filed
25 with regard to, for example, their plant in service

1 claim, I mean, there are pages and pages and pages of
2 project data with code numbers, you know, and, I mean,
3 there's a lot of data in this case, but, in my view,
4 sometimes less is more, and I think the information
5 could be organized in a manner or perhaps summarized in
6 a manner that would be more helpful. For example, I
7 found Ms. Bridwell's testimony, I believe it was, with
8 her description, she actually gave you a short project
9 description narrative of the company's major projects.
10 I found that very helpful. So I think there are ways
11 that you can summarize this data that facilitates
12 review, you know, and I would hope that we would get
13 there, especially because I understand that there's
14 some discussion of going to a paperless filing, and,
15 you know, as a consultant, I would beg the Commission
16 not to go there, because, when you're looking at these
17 files that come in, somebody has to print these filings
18 out. It's not like they just sit there on the
19 computer, and I can't, at least, sit and go through
20 thousands of pages on my computer. I mean, I don't
21 know many people that operate that way, and so, if
22 you're talking about voluminous filings that could be
23 organized, you know, in ten different ways, please give
24 us at least one paper copy so that we know we have
25 everything that's been provided. So there are some of

1 my thoughts in that regard.

2 Q. Well, as one of the persons within the Commission Staff
3 that have been advocating the paperless rate case, I
4 might take exception to your comments, but let me ask,
5 are you aware of any utility regulatory commission that
6 has adjusted or disallowed a portion of rate case
7 expense as a result of what it deemed to be the poor
8 quality of a filing or response to parties' or
9 regulatory commissions' requests for information? By
10 that, I mean explicit as opposed to implicit, an
11 explicit disallowance.

12 A. Not that I can think of; no.

13 Q. Let's talk about security costs for a few minutes. I
14 believe you testified earlier today that you had not
15 reviewed the reasonableness of the security costs that
16 are part of the deferred security costs issue; is that
17 correct?

18 A. Well, I stated that I didn't review them in the same
19 level of detail as I might have had I been inclined to
20 allow some of them to be recovered, some of the
21 deferred costs to be recovered. I certainly looked at
22 them. You know, I looked at them. I looked at the
23 components that were included, but I did not come up
24 with a recommendation with regard to the reasonableness
25 of every cost included therein.

1 Q. Okay, and I think you had mentioned that one of the
2 reasons for a more limited review was your position
3 that, since the company had not received approval to
4 defer those expenses, the requested ratemaking
5 treatment should be disallowed; is that correct?
6 A. Right, and the fact that these costs had, in fact, come
7 up before, you know, in the merger case.
8 Q. Okay. Well, let's step back a second. I want you to
9 assume something now. Let's assume, for the moment,
10 the company has made the proper request for that
11 deferral and the deferral is before this Commission.
12 A. Uh-huh.
13 Q. What criteria would you suggest to the Commission ought
14 to be used to determine whether the deferral should be
15 granted?
16 A. Okay. I'm not a big fan of deferrals, to begin with.
17 So I think that the deferral should be so material that
18 the financial integrity of the company is in jeopardy.
19 Q. Okay. Can I stop you there?
20 A. Sure.
21 Q. When you say "material," are we talking about the same
22 notion materiality that an outside or external auditor
23 would use in looking at a utility's financial
24 statements?
25 A. Well, not necessarily. I think we talked about - I

1 think 10 percent was the number that I heard the other
2 day that was used . . .

3 Q. Yes, ma'am.

4 A. . . . by the auditors, and I don't have a particular
5 percentage in mind, but I think deferrals should be
6 used in very, very rare instances where you have a cost
7 that is outside the control of the company that would
8 cause the company to suffer very serious financial
9 consequences if it were not permitted to be reflected
10 in rates. This is assuming, of course, that the
11 company had come in and received deferred accounting
12 treatment.

13 Q. All right. In your opinion, would the circumstances
14 surrounding the occurrence of the security costs that
15 we've discussed the last few days, would that be
16 considered rare or extraordinary or outside the control
17 of the utility?

18 A. Certainly, it would be considered rare and extra-
19 ordinary and certainly, to some extent, outside the
20 control of the utility. Certainly, the utility had the
21 ability to make various decisions about the way it was
22 going to react to the events of September 11th.
23 However, I don't think it would meet the test of
24 materiality in this case.

25 Q. And why is that?

1 A. Well, you're talking about, for example, in this case,
2 a rate increase, you know, on the magnitude of, what,
3 \$7.3 million. You know, that's roughly, what, a
4 16 percent increase, 16-17 percent increase. I mean,
5 I'm just looking at the ability of the company to
6 absorb the types of costs that, in fact, it incurred as
7 a result of September 11th, and, you know, to be
8 honest, that's why shareholders receive a return on
9 equity, because there are unforeseen events, many of
10 them outside the control of the company, that do occur
11 from time to time, and the magnitude of the costs that
12 we're faced with here, I think the security piece - I
13 think the amount that came out of rate base was
14 somewhere in the neighborhood of, yeah, \$2.7 million is
15 the unamortized piece. So the total costs would be
16 slightly higher than that. You know, I don't view that
17 as the type of event, in my view, that would warrant
18 deferred treatment, and, again, that's . . .

19 Q. Okay.

20 A. Philosophically, I'm not a big fan of deferrals.

21 Q. Okay. You mentioned the ability to absorb, and a
22 utility regulatory commission, reviewing a utility's
23 ability to absorb these types of increases, should the
24 Commission take into account any action on the part of
25 a utility to defer or refrain from asking for rate

1 adjustments or specific tariff riders that might
2 provide recovery for those costs in determining whether
3 the utility has the ability to absorb those costs?
4 A. Sure. I mean, in this case, this is not a new cost.
5 These costs were known, early on. The company, in
6 2001, filed for a surcharge. They withdrew that
7 surcharge, litigated the merger case as a - you know,
8 if these costs were so material to the company that
9 they had to have recovery, it seems to me that they
10 should have brought that to the Commission's attention
11 when they signed off on Condition No. 2, which
12 indicated that they would not seek recovery of these
13 types of costs until their next rate case. They
14 didn't. They were silent on that issue. I mean, the
15 company knew that these costs were out there, and they
16 chose not to sort of make that an issue in the merger
17 case. So, fine. I think it's a little late now to be
18 bringing them up and saying, "Well, we thought all
19 along that we had the right to defer these costs and to
20 seek recovery in this case." I mean, these should have
21 been discussed fully in that case if the company felt
22 they were so material.

23 MR. WUETCHER:

24 Your Honor, I see by my monitor that it's almost
25 twelve-thirty, and we are somewhat at a good

1 break . . .

2 CHAIRMAN GOSS:

3 You must be hungry, Mr. Wuetcher.

4 MR. WUETCHER:

5 Pardon me, sir?

6 CHAIRMAN GOSS:

7 You must be hungry.

8 MR. WUETCHER:

9 No, sir, not really, but . . .

10 CHAIRMAN GOSS:

11 I'm kidding with you, Mr. Wuetcher. Okay. Are

12 you at a good breaking point?

13 MR. WUETCHER:

14 Yes, sir.

15 CHAIRMAN GOSS:

16 All right. Let's break, then. Has the hour and a

17 half lunch been too long or been about right in

18 terms of getting fed and getting back?

19 MR. SPENARD:

20 Mr. Chairman, it has been. Our main concern,

21 though, is that we would like to make sure that

22 this witness is finished today.

23 CHAIRMAN GOSS:

24 We're going to finish this witness today.

25

1 MR. SPENARD:

2 All right.

3 CHAIRMAN GOSS:

4 I can assure you of that.

5 MR. SPENARD:

6 Okay. That's fine.

7 CHAIRMAN GOSS:

8 All right. Mr. Howard?

9 MR. HOWARD:

10 No, sir. I was just . . .

11 CHAIRMAN GOSS:

12 Okay. Let's take an hour and fifteen minutes.

13 Fridays can sometimes be a little difficult in

14 Frankfort getting something to eat, but I think

15 maybe we can do it in an hour and fifteen minutes.

16 Let's come back at one forty-five, then; okay?

17 We'll be in recess until then.

18 OFF THE RECORD

19 CHAIRMAN GOSS:

20 Please be seated. Okay, Mr. Wuetcher.

21 MR. WUETCHER:

22 Thank you, Your Honor.

23 Q. Good afternoon, Ms. Crane.

24 A. Good afternoon.

25 Q. Are you aware of the Commission's past treatment of

1 depreciation expense with regard to its inclusion in
2 the calculation of working capital?
3 A. For Kentucky-American, I am; yes.
4 Q. Okay, and would it be correct to say that that position
5 has been that depreciation expense is included in rate
6 base with regard to the calculation of working capital?
7 A. Yeah, depreciation is included in cash working capital
8 which is a component of rate base.
9 Q. Okay. We previously talked about the regulatory
10 proceedings where you appeared as a witness. In any of
11 those proceedings, have you recommended that
12 depreciation expense be included in the lead-lag
13 calculation of working capital?
14 A. No, although New Jersey is the only state I know, in
15 addition to Kentucky, that does include depreciation
16 expense in cash working capital. I may have filed a
17 testimony there where I was silent on the issue, but I
18 have not recommended that it be included in any state
19 that I can recall.
20 Q. Okay. I believe, in this proceeding, there has been
21 testimony given regarding the inclusion of depreciation
22 expense in the calculation of working capital of other
23 American Water Works Company subsidiaries, and I think
24 you just testified that New Jersey allows the
25 inclusion. To your knowledge, do you know why New

1 Jersey allows that type of treatment?

2 A. I haven't a clue.

3 Q. Is it correct, in all the other jurisdictions in which

4 American Water Works subsidiaries operate, aside from

5 Kentucky and New Jersey, depreciation expenses is not

6 included in the calculation of working capital?

7 A. I haven't testified in every jurisdiction in which

8 there's an American Water Company operating. So I

9 can't personally speak for every jurisdiction. I'm not

10 aware of any other jurisdiction that includes depre-

11 ciation expense in cash working capital other than New

12 Jersey.

13 Q. Okay. Your statement, would that cover not only

14 jurisdictions in which American Water Works companies

15 operates but the remaining jurisdictions in the

16 country?

17 A. Yes. I'm not aware of any.

18 Q. Okay. At I believe it's Page 77 of your testimony, you

19 touch upon the subject of normalization versus

20 amortization of deferred maintenance.

21 A. Yes.

22 CHAIRMAN GOSS:

23 What page is that, Mr. Wuetcher?

24 MR. WUETCHER:

25 Page 77.

1 CHAIRMAN GOSS:

2 Okay. Thank you.

3 Q. Under normalization, would the unamortized deferred
4 maintenance balances be included in rate base?

5 A. No. There would be no unamortized deferred balances if
6 normalization is used.

7 Q. Other than their exclusion from rate base and the
8 related deferred tax issues, what is the difference in
9 normalization as presented in your testimony and
10 amortization as presented in Kentucky-American's
11 Application?

12 A. Amortization is the future recovery of a previously
13 incurred cost. So you're looking at a cost that was
14 actually incurred, and you're saying, "I'm going to
15 give the company recovery of this amount in future
16 rates over some period of time." With normalization,
17 you're not looking at recovery of a past cost. You're
18 saying, "On a normal prospective basis, what is the
19 likely or expected annual amount that this company is
20 going to incur for this expense?" Now, the dollar
21 amounts may not vary, because, frankly, in order to
22 determine a reasonable prospective amount, commissions
23 generally do have to go back and look at past amounts
24 and then they make some determination as to whether or
25 not, you know, they think that the past amounts are

1 reflective of the future. So the numbers can be
2 different, the number of the overall allowance,
3 although they don't have to be different but they can
4 be different, and it's really the perspective of
5 recovery of a past cost versus recovery of a future
6 cost.

7 Q. Would you agree with the statement, "Deferred
8 maintenance is a common concept in ratemaking"?

9 A. No, I wouldn't.

10 Q. Can you explain that, your response?

11 A. Sure. I haven't seen many jurisdictions that permit
12 deferred maintenance, as I believe you're using the
13 term here, which is the way it's reflected in Kentucky-
14 American's case. I have seen - I would say that there
15 are some jurisdictions that specifically amortize tank
16 painting expenses, which is one component, as I
17 understand it, of the company's claim here, but, in
18 terms of the other areas of maintenance, generally what
19 commissions are looking at is what is a normal
20 prospective expected level of maintenance, you know,
21 that we think is reasonable to include in rates. So
22 it's not a cost that, in my experience, is amortized by
23 very many commissions with the exception, as I stated,
24 tank painting in some jurisdictions is.

25 Q. Okay. Is it customary for other regulatory commissions

1 to include the unamortized deferred maintenance
2 balances in rate base?
3 A. No.
4 Q. For example, . . .
5 A. I would say . . .
6 Q. Well, let me rephrase that.
7 A. I'm sorry.
8 Q. My question is being altered as we speak. Is it
9 customary for other regulatory commissions to include
10 the unamortized deferred maintenance balances in rate
11 base where we're speaking of, for example, tank
12 painting?
13 A. No. It would be amortized with no rate base treatment.
14 Q. Would you agree that CWIP in rate base and AFUDC above
15 the line, as proposed in Kentucky-American's
16 Application, results in Kentucky-American receiving a
17 return on non-AFUDC bearing CWIP only and not the
18 entire CWIP balance?
19 A. Well, they receive a return on the entire CWIP balance.
20 There is an offset which is an AFUDC offset. So the
21 net effect is the same as if they were only receiving a
22 return on the non-AFUDC CWIP.
23 Q. Would you agree that your adjustment related to CWIP
24 taxed the revenue requirement by \$132,000 as calculated
25 by Mr. Miller?

1 A. I believe that I actually answered a data request
2 response on that, and it was very close to that number.
3 It might have been \$134,000. I would agree that that's
4 the ball park.

5 Q. Okay.

6 A. It probably depends, too - you know, obviously, it will
7 depend, for example, on what overall cost of capital
8 you assume. So, you know, there's not one number. It
9 is going to depend on what overall cost of capital you
10 use. When I did my calculation, I used my overall cost
11 of capital.

12 Q. Okay. You proposed to reduce forecasted payroll on the
13 basis that Kentucky-American currently has three vacant
14 positions; is that correct?

15 A. Well, they did have three vacant positions. Now, they
16 have 14.

17 Q. Okay. Well, let me go ahead. You've read the rebuttal
18 testimony of Mr. Bush where he explains how the vacant
19 positions and overtime hours are counted for through
20 the budgeting process?

21 A. Yes, I have read that.

22 Q. And have you reviewed Kentucky-American's Response to
23 the Item 20 of the Commission Staff's Fourth Set of
24 Information Requests to Kentucky-American where
25 budgeted versus actual overtime hours are compared?

1 A. I believe so. I don't remember the number, but I do
2 recall a response that showed that for a number a
3 years, the actual versus budget. I presume that's what
4 you're referring to.

5 Q. Yes, ma'am.

6 A. Yes.

7 Q. Okay. Does Mr. Bush's testimony and Kentucky-
8 American's response to that information request change
9 your position and recommendation on this matter?

10 A. No.

11 Q. If a company budgets assuming that all employee
12 positions will be filled during an operating period and
13 overtime is projected based on that assumption, is it
14 reasonable to assume that, if actual employee levels
15 are not at capacity, the overtime hours would then
16 increase for the actual employees?

17 A. I would say that that would be a general expectation.
18 However, I don't think that it follows that the overall
19 costs are going to remain unchanged. I mean, the fact
20 is this company, like most utilities, pretty much
21 always has vacancies, and, while it's true that you are
22 probably going to use more temporary employees and
23 incur more overtime costs, you know, there's not
24 necessarily a dollar for dollar offset. I mean, the
25 company has testified that management employees, for

1 example, don't get overtime. So they may have to just
2 work a little harder without additional compensation.
3 So you cannot then assume that their costs are going to
4 remain unchanged because they have filled this need
5 through the use of temporary labor and overtime.

6 Q. Okay. Does your proposed adjustment consider
7 additional overtime required of actual employee levels
8 to make up for the vacant positions?

9 A. I didn't make an adjustment, if that's what you're
10 asking for, but I think my adjustment is conservative.
11 It was three positions, and now they're up to 14, and
12 it sounds like there's still some reorganization going
13 on, so I think my adjustment is still reasonable.

14 Q. You recommended some proposed adjustments related to
15 the expenses associated with Kentucky-American's
16 President's office; did you not?

17 A. Yes, I did.

18 Q. And those were primarily related to the President of
19 Kentucky-American being involved in any - I don't want
20 to use the term "battle" - let me use the term "any
21 litigation" or movement to address condemnation efforts
22 that were being brought by Lexington-Fayette Urban
23 County Government; is that correct?

24 A. For the salary piece of that, yes. There was also an
25 incentive comp adjustment.

1 Q. Would it be correct to say that that adjustment - well,
2 would it affect your adjustment if there were changes
3 made in the position taken by the Lexington-Fayette
4 Urban County Government regarding proceeding with
5 condemnation proceedings?
6 A. Well, it could, although I understand that that
7 President isn't even here anymore; that's there's a new
8 President who isn't doing this full-time yet. You
9 know, maybe he will be at some point in the future.
10 So, you know, all other things being equal, yes, that
11 would be an interesting piece of information to have,
12 but I don't think that, at this point in time, that's
13 the sole consideration.
14 Q. Your proposed adjustment raised an interesting
15 question. Let's assume for the moment we're not
16 talking about condemnation efforts, . . .
17 A. Uh-huh.
18 Q. . . . but let's say the President of Kentucky-American
19 is heavily involved in the local United Way . . .
20 A. Uh-huh.
21 Q. . . . and apparently has to devote a certain number of
22 hours to ensuring a successful United Way Campaign.
23 A. Uh-huh.
24 Q. I assume you would take the position that the time and
25 effort that that person directs to the United Way

1 Campaign is a time for which the ratepayers should not
2 be required to pay even a portion of his salary; would
3 that be correct?

4 A. In spite of the admirable goal of the United Way, yes,
5 that would be my position.

6 Q. Okay. In terms of actually setting the rate or making
7 the adjustment, how is the Commission, in that circum-
8 stance or in a circumstance similar to that, to make
9 the adjustment if, let's say, for example, the period
10 in which that person will serve as the Chairman of the
11 United Way Campaign is in the projected or forecasted
12 test period as opposed to, let's say, the historical
13 test period? In other words, I guess what I'm getting
14 at is how to determine the amount of the adjustment if
15 you believe an adjustment is necessary.

16 A. Well, if you know about the circumstances, you know,
17 obviously you would have to do the best job that you
18 could in terms of estimating what you think is a
19 reasonable amount of time that that person would spend
20 and what percentage of that time that was, and then you
21 would have to take that percentage and multiply it by
22 their weighted wage rate with, you know, benefits and
23 everything else involved. You know, the bigger
24 difficulty is determining that that's actually going to
25 take place, because, of course, that's a piece of

1 information that may very well never come out in a
2 review of a rate case, you know, of this size unless
3 the company somehow identifies, you know, that that's
4 going to take place.

5 Q. Would it be correct to say, then, that, in an area like
6 that, it highlights the problems with a future test
7 period?

8 A. It certainly does

9 Q. You've proposed the elimination of Service Company
10 charges that are related to business development costs?

11 A. Yes.

12 Q. In your opinion, do Kentucky-American customers benefit
13 from Kentucky-American exploring business development
14 opportunities to grow its customer base?

15 A. There could be some benefits to existing customers of
16 things like the acquisition of new systems or other
17 business development opportunities. On the whole,
18 though, I think the dangers of permitting those types
19 of costs in rates far outweigh any subsequent benefits
20 and therefore I would not deny that there could be some
21 benefits, but I don't think those costs should be
22 included in rates.

23 Q. Okay. To follow up on that question, could you
24 identify for us what you believe the potential benefits
25 might be and what the dangers are?

1 A. Sure. Well, you know, generally speaking, all other
2 things being equal, one assumes that there are
3 economies of scale. Now, you know, I mentioned earlier
4 that's not always the case because sometimes you're
5 bringing in a little system that doesn't need all the
6 bells and whistles, you know, of your infrastructure,
7 but, you know, generally speaking, I would agree that
8 one expects that there are going to be economies of
9 scale as you bring in new systems. I think the danger
10 is that you provide a significant incentive for the
11 utility to be spending its resources basically in
12 growing itself and, I mean, let's not forget how the
13 shareholders are rewarded. I mean, there's only really
14 one way that a shareholder gets to increase the amount
15 that they get, and that is by growing rate base. I
16 mean, that's it for a regulated utility. You know, if
17 you grow rate base, you get a bigger return, you know,
18 all other things being equal, and there really isn't
19 any other way to get a bigger return. So it's to the
20 benefit of shareholders to have as large a rate base as
21 they possibly can, and, in many situations, that means
22 going out and acquiring new systems. With regard to
23 the management - and, you know, frankly, sometimes they
24 acquire the systems and aren't too concerned about what
25 they have to pay to get them, especially if they think

1 that any acquisition premium is also going to be
2 included in rate base. So they'll still be better off.
3 From a management perspective, you know, unfortunately,
4 I guess, we all like to feel that we are, you know, in
5 charge of a bigger, you know, fiefdom, and, frankly, to
6 the extent that you take a utility manager and you can
7 grow that utility and give him or her, you know, more
8 power, more authority, I mean, I think that's another
9 incentive for a utility to go out and acquire other
10 utilities. So there are a couple of incentives to do
11 that, and, you know, I don't have any problem with
12 acquisitions. I mean, I think they can be very
13 valuable, especially for smaller companies that maybe
14 don't have access to all the resources of a big
15 company. So I'm not opposed to that, but you have to
16 make sure that your existing customer base, you know,
17 isn't paying for that, and I think allowing business
18 development costs for a regulated company, you know, I
19 don't think that's reasonable or appropriate.

20 Q. You proposed an adjustment for a consolidated tax
21 filing; is that correct?

22 A. Yes, I did.

23 Q. And Mr. Ingram has already questioned you on that. I
24 just have a couple of questions in regard to that
25 proposal.

1 A. Okay.

2 Q. In terms of developing that proposal, did you take into
3 consideration any of the conditions or requirements
4 that the Commission had imposed upon RWE and its
5 subsidiaries as a part of approving the transfer of
6 control of Kentucky-American from American Water Works
7 Company to RWE?

8 A. Well, I think basically consolidated income tax
9 adjustments are a good thing and should be adopted,
10 period. In this case, there was sort of an additional
11 reason for recommending a consolidated income tax
12 adjustment and that was the Commission's Order in the
13 merger case, you know. I wasn't involved in that case,
14 but it's my understanding that the company came in and
15 revised its petition to include a different organi-
16 zational structure, and the reason they wanted to do
17 that was so that they could take advantage of a
18 consolidated income tax structure or filing, and I'm
19 also aware that the Commission ordered that savings
20 related to the merger be tracked, and so I think
21 there's sort of an added reason in this particular case
22 for adopting a consolidated income tax adjustment.

23 Q. I believe I have one more question. In his testimony,
24 both his filed testimony and in his testimony here a
25 few days ago, Dr. Spitznagel gave several reasons

1 regarding why he believed Kentucky-American's customers
2 were consuming water at a lower rate. In particular,
3 he made reference to improved water fixtures and
4 appliances. Do you agree that improved water fixtures
5 and appliances would create a drop in the average
6 consumption of Kentucky-American's residential
7 customers?
8 A. Yes, but not to the extent that Dr. Spitznagel has
9 suggested. When I look at the numbers, Kentucky-
10 American is growing, according to the company, roughly
11 2.5 percent a year in customers, in number of
12 customers. Dr. Spitznagel states the consumption has
13 declined. Consumption per customer has declined
14 somewhere in the magnitude of 10 percent since its last
15 case. If you run through the numbers and you assume
16 that all the customers that you had at the time of the
17 last case are still using the same amount of water, -
18 assume that they did not get new fixtures, and I know
19 some of them did, but the company claims that there's a
20 lot of growth with new customers, new developments, and
21 new fixtures - if you assume that your old customers
22 are using exactly the same amount of water, your new
23 customers would have to be using essentially no water
24 in order to come up with a 10 percent reduction in per
25 customer consumption. That simply does not make sense.

1 So I think, when you're looking at a statistical model,
2 at the end of the day, you have to ask yourself do the
3 results make sense, and that does not make sense. If
4 you look at my numbers and you assume 2.5 percent
5 growth, roughly, in customers, my model would suggest
6 that all these new customers are using roughly 50 per-
7 cent of the water that, what I'll call, the old
8 customers or the prior customers were using. My
9 recommendation results in about a 5 percent decline in
10 consumption per customer since the last case. Frankly,
11 I think that a 50 percent drop, you know, is probably
12 too big of a drop. Maybe the company's revenue is
13 actually even greater than I am recommending in this
14 case, but certainly, you know, I think my recom-
15 mendation where your new customers are using roughly
16 50 percent of the water that your prior customers used
17 is much more reasonable than Dr. Spitznagel's. When
18 you go through his numbers and you put it on a
19 practical basis, I mean, they just don't add up, and,
20 you know, I'm not faulting his model per se, but, at
21 the end of the day, you have to say, "Does this model
22 make sense?" and I don't think his does.

23 Q. Let me follow up with one question on that. When you
24 take into account or you make the assumption that old
25 customers have not changed their consumption patterns

1 or have not placed in new fixtures or appliances that
2 would result in improved water savings . . .
3 A. Uh-huh.
4 Q. . . . or less water consumption, are you also taking
5 into account the industrial or large commercial
6 customers that might have an incentive to reduce their
7 water usage?
8 A. No. That example I just gave you was purely a
9 residential example.
10 MR. WUETCHER:
11 I believe that's all we have. Thank you, Ms.
12 Crane.
13 A. Thank you.
14 CHAIRMAN GOSS:
15 Does the Commission have any questions?
16 EXAMINATION
17 BY CHAIRMAN GOSS:
18 Q. I want to understand something that I thought you said
19 earlier under cross examination by Mr. Ingram. I
20 understand your dislike for deferred accounts, but,
21 putting that aside for a minute, with regard to this
22 security cost issue, . . .
23 A. Uh-huh.
24 Q. . . . did I understand you to say that you did not
25 disagree with the reasonableness or you did not

1 question the reasonableness of the amounts expended by
2 the company for security for the period of time that
3 we're talking about?

4 A. Yes. I also said, however, that I did not do an in-
5 depth review of those amounts since I was going to
6 suggest that there be no deferral permitted, but I am
7 not taking issue with any specific expenditure, you
8 know, claimed by the company in that regard.

9 Q. Well, I guess I would like to know how in-depth your
10 review of those numbers were.

11 A. Uh-huh.

12 Q. I mean, did you just look at them and sort of eyeball
13 them and say, "Well, it looks okay to me," or did you
14 actually concentrate on it for a little while and run a
15 few things out, or do you recall what you did in terms
16 of the reasonableness of those numbers?

17 A. Sure. You know, I did more than just sort of glance at
18 them. I mean, I looked at the categories of costs and
19 the capital versus the operating costs that have been
20 incurred. I was certainly aware of what I'll call the
21 three stages of guards with regard to the police coming
22 in first really as policemen and then going to Alliance
23 and then going to the guard system and the relative
24 costs of each of those three options, those sorts of
25 things. I did not, though, go a step further and say,

1 "Okay. Should the company really have called in all
2 those policemen on September 12?" You know, "Was the
3 company correct when it made the decision that it was
4 now going to use Alliance to administer that process?
5 Is there some less expensive way that they could have
6 obtained the same result?" You know, I didn't really
7 try and get behind their thought processes and whether
8 there were other options that perhaps would have been
9 better. You know, I didn't explore, "Well, should they
10 have made more of an effort to get National Guardsmen
11 down here perhaps, you know, at less costs?" So I
12 didn't really question their motives behind their
13 expenditures. I did look at the expenditures and say,
14 "These look, you know, relatively in line with the
15 services that they obtained," but I didn't question
16 whether they made the right decisions about whether or
17 not to obtain those services.

18 CHAIRMAN GOSS:

19 All right. Okay. I'll turn it back to you, Mr.
20 Spenard, for redirect.

21 MR. SPENARD:

22 Yes. Thank you, Mr. Chairman. We have no
23 redirect examination.

24 CHAIRMAN GOSS:

25 Okay. Thank you. Mr. Ingram, do you have any

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recross?

MR. INGRAM:

A few, Your Honor.

MR. SPENARD:

Mr. Chairman, . . .

CHAIRMAN GOSS:

Uh-huh.

MR. SPENARD:

. . . playing by the rules we played by yesterday while the Office of the Attorney General was cross examining their witnesses, there was no recross outside of the scope of redirect.

CHAIRMAN GOSS:

Oh, no, it's - oh, I see what you're saying. Well, that's true. Let me ask a question. I'm relatively new at this. This is only about my third or fourth hearing. What has been the rule of practice in the Commission when we have had multiple - I believe I struck a nerve - when we've had multiple parties? In other words, rather than just having an applicant and a consumer representative and the PSC, we have obviously other intervenors. Let me ask you, first, Mr. Spenard. What's been the practice?

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MR. SPENARD:

Well, and I want you to bear with me for just a second, is that the practice is changing, evolving, and I think that I learned a lesson on surrebuttal, which is fine. I think it was a good lesson. So I'm trying as best I can to play by the rules that you're announcing and not looking at what we've done in the past and say that automatically applies and, with regard to the cross, my understanding of listening yesterday when their witnesses were on the stand is that there was a scope limitation. So, with regard to what the past practice has been, for example, with surrebuttal, I thought that your all's ruling and Order on the 27th about surrebuttal was really good in saying, "Regardless of how you've done it in the past, we're going to lay it down," because, in the past, I used to ask the witness if they've sat through the hearing, if they've heard anything, do they have any additional comments, and things like this, and we didn't do it this time, which is fine, and those are the rules, and, again, I was just listening to what you did yesterday and say, "Well, if this is how we do it, this is how we do it."

1 CHAIRMAN GOSS:
2 You're exactly right. It was limited to the
3 scope. Mr. Ingram, do you want to respond?
4 MR. INGRAM:
5 I have a response to the question, Your Honor, and
6 I also have something else to say. There are
7 generally no rules of evidence in front of the
8 Public Service Commission.
9 CHAIRMAN GOSS:
10 Yeah.
11 MR. INGRAM:
12 However, I will make this decision real easy. I
13 have no further questions for Ms. Crane.
14 CHAIRMAN GOSS:
15 Okay. All right.
16 CHAIRMAN GOSS:
17 Let me just ask a question while we're in this. I
18 mean, I'm sort of learning as I go. Obviously,
19 I've been where you all have been for a number of
20 years, and I'm used to sort of doing it that way.
21 Does the Bar prefer that it be a little less
22 strict, a little less stringent, in terms of
23 limiting recross to the scope of redirect, or do
24 you all - Mr. Howard?
25

1 MR. HOWARD:

2 Mr. Chairman, today . . .

3 CHAIRMAN GOSS:

4 This is just for my own edification.

5 MR. HOWARD:

6 Sure. In my roughly 11 years of practice here,
7 the deference has always been given to the
8 Commissioners to establish the rules. Now, true,
9 and I've practiced before many administrative
10 bodies, the rules of evidence are relaxed. The
11 rules of procedure are relaxed, and, again, great
12 deference is given to, in this case, the tribunal.
13 Once we have a change of rules, then, unless
14 there's a compelling argument to deviate from the
15 requested deviation, . . .

16 CHAIRMAN GOSS:

17 Uh-huh.

18 MR. HOWARD:

19 . . . that we adhere to that and that's why
20 yesterday, once the issue came up about, well, you
21 have to limit the recross to redirect, frankly, I
22 don't believe that I had witnessed that here up
23 until then, but such was the rule and obviously we
24 were bound to abide by that. Now, I think Mr.
25 Ingram - what he was going to say and was

1 suggesting is that, in the past, yes, if there are
2 multiple parties, you were able to go outside of
3 the realm of redirect and get into additional
4 recross, but it appears as though the lay of the
5 land has now changed.

6 CHAIRMAN GOSS:

7 Well, this is a work in progress, guys. I want to
8 be fair. I want every attorney to have an
9 opportunity to feel like due process has been
10 given by the Commission. This is not a circuit
11 court. It's not a federal court. It is an
12 administrative body, and I intend - things are
13 relaxed, and I want to give the Bar an opportunity
14 to ask all the questions they want to ask and to
15 get to the nut of the thing, and, by limiting
16 recross to the extent of redirect in this case,
17 I'm not saying that's going to be any sort of
18 future pronouncement or future scheme that we go
19 by here. It helps me to know that it's been maybe
20 not quite that strict and stringent before. I'm
21 certainly willing - all I'm trying to do by doing
22 that is narrow the thing down each time I go
23 around the table to where I don't open it up for,
24 you know, another hour's worth of examination. If
25 the Bar prefers to have it a little more loose and

1 a little more relaxed, I'm perfectly comfortable
2 with that. I think it is fair and it is only
3 proper for me to be consistent in this case.
4 Since I did limit it with regard to one side, it
5 needs to be that way for the other. Mr. Ingram
6 indicated he had no questions. So it's not really
7 an issue, but, now knowing and hearing from the
8 Bar what you all prefer - do you echo that, Mr.
9 Childers?

10 MR. CHILDERS:

11 I would agree that this is a relaxed proceeding
12 and that . . .

13 CHAIRMAN GOSS:

14 Okay.

15 MR. CHILDERS:

16 . . . typically there ought to be adequate
17 opportunity to ask all the questions, . . .

18 CHAIRMAN GOSS:

19 Okay. All right.

20 MR. CHILDERS:

21 . . . and the strict rules of evidence and
22 procedures should not apply.

23 CHAIRMAN GOSS:

24 Okay.

25

1 MR. INGRAM:

2 You know, Your Honor, even in circuit courts or
3 federal courts, I think I have never seen an
4 opportunity or a situation where, on recross, I
5 would say, "Your Honor, I forgot to ask three or
6 four . . ."

7 CHAIRMAN GOSS:

8 Right. Right.

9 MR. INGRAM:

10 ". . . questions. Could I be permitted to ask
11 those?" that I haven't been permitted to ask them.

12 CHAIRMAN GOSS:

13 Right.

14 MR. INGRAM:

15 I think, as I told the, for lack of a better word,
16 auditor of the PSC process who called me up
17 yesterday for my input on the PSC, the whole
18 purpose of this proceeding is to get a fully
19 developed record for intelligent and well
20 thought-out decisions, and, if there are materials
21 that are not in the record because I forgot them
22 or anybody else forgot them, they ought to be put
23 in the record.

24 CHAIRMAN GOSS:

25 Yeah, I agree with that.

1 MR. INGRAM:

2 That's the bottom line of my thinking about the
3 subject.

4 CHAIRMAN GOSS:

5 Okay. Well, I appreciate the . . .

6 MR. HOWARD:

7 Mr. Chairman, I would concur with that, but it's a
8 matter of how far do we go. Do we have recross
9 and we open up a whole new area of recross, and
10 then do we have yet another re-recross? It could
11 go on indefinitely. So I think that there are
12 certain limitations that need to be made, but we
13 want to have a complete record.

14 CHAIRMAN GOSS:

15 Well, I can certainly - since I'm presiding, I can
16 take care of that by just, you know, indicating
17 that that's redundant information, we've plowed
18 that ground before, but I think probably, after
19 this hearing is concluded, I'll maybe loosen up a
20 little bit and just let everybody sort of -
21 because you all are very good attorneys and very
22 accomplished and have a lot of experience, and you
23 know what you're supposed to do and what you're
24 not supposed to do. So I appreciate that counsel
25 from you all.

1 MR. HOWARD:
2 Okay. Thank you.
3 CHAIRMAN GOSS:
4 Do you agree with that, Mr. Wuetcher?
5 MR. WUETCHER:
6 Yes, sir.
7 CHAIRMAN GOSS:
8 Okay. All right. Okay.
9 MR. SPENARD:
10 With that, we would ask if this witness can be
11 excused.
12 CHAIRMAN GOSS:
13 Yeah. Yes, Ms. Crane, thank you. You may step
14 aside.
15 A. Thank you.
16 CHAIRMAN GOSS:
17 Okay. According to my list, Mr. Spenard, that
18 concludes your witnesses for today; is that
19 correct?
20 MR. SPENARD:
21 Yes, Mr. Chairman.
22 CHAIRMAN GOSS:
23 Okay. Now, let's see. Mr. Childers, was it you -
24 you had a witness, but everybody agreed that they
25 didn't have any questions, and I told you not to

1 bring that witness; is that right?
2 MR. CHILDERS:
3 Mr. Burch, and he has prefiled his testimony,
4 and . . .
5 CHAIRMAN GOSS:
6 Okay.
7 MR. CHILDERS:
8 . . . he has no changes to that testimony. We
9 would ask that it be admitted, Your Honor.
10 CHAIRMAN GOSS:
11 Okay. That is admitted of record. All right. So
12 that leaves Dr. Vander Weide that we're assuming
13 we're going to be able to do that on the 23rd
14 unless we're told differently and, certainly, if
15 there's a snafu somehow or a problem, why, we can
16 adjust. All right. We've indicated previously, I
17 think, that briefs would be due, what did I say,
18 the 7th?
19 REPORTER:
20 The 4th of January.
21 CHAIRMAN GOSS:
22 The 4th of January and then replies - that's
23 simultaneous briefs, simultaneous replies - would
24 be due by January the 11th. Okay. Are there any
25 other matters that the Commission needs to take up

1 at this time before we adjourn?

2 MR. INGRAM:

3 I don't think so, Your Honor, but I would simply
4 say I think there's an agreement among counsel now
5 as to the hearing data requests. We prepared that
6 list, and there's been some discussion about it.
7 If anybody wants to make some changes about it
8 after this, if you will just let us know, we'll
9 proceed accordingly.

10 CHAIRMAN GOSS:

11 All right.

12 MR. INGRAM:

13 And they'll be due ten days from today?

14 CHAIRMAN GOSS:

15 Yes, correct. I thank you all very much for
16 appearing. Everyone did a great job. I thank all
17 the witnesses for coming. I apologize to Ms.
18 Crane for making you wait around an extra day.
19 It's probably a lot colder in Connecticut than it
20 is here, though. So maybe things didn't work out
21 so bad. Okay. If there's nothing else, then, to
22 take up, the Commission will be in adjournment.

23 FURTHER THE WITNESSES SAITH NOT
24 HEARING ADJOURNED
25 OFF THE RECORD

1 STATE OF KENTUCKY
2 COUNTY OF FRANKLIN

3
4 I, Connie Sewell, the undersigned Notary Public, in
5 and for the State of Kentucky at Large, do hereby
6 certify the foregoing transcript is a complete and
7 accurate transcript, to the best of my ability, of the
8 hearing taken down by me in this matter, as styled on
9 the first page of this transcript; that said hearing was
10 first taken down by me in shorthand and mechanically
11 recorded and later transcribed under my supervision;
12 that the witness was first duly sworn before testifying.
13 My commission will expire November 19, 2005.

14 Given under my hand at Frankfort, Kentucky, this the
15 2nd day of December, 2004.

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Connie Sewell

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