COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ADJUSTMENT OF THE RATES OF KENTUCKY-AMERICAN WATER COMPANY	))	CASE NO. 2004-00103

<u>COMMISSION STAFF'S SECOND SET OF INFORMATION REQUESTS TO KENTUCKY-AMERICAN WATER COMPANY</u>

Pursuant to Administrative Regulation 807 KAR 5:001, Commission Staff requests that Kentucky-American Water Company ("Kentucky-American") file the original, one copy in paper medium and one copy in electronic medium of the following information with the Commission no later than June 28, 2004, with a copy to all parties of record. The electronic copy shall conform to the provisions of the Commission's Order of May 27, 2004. Each paper copy of the information requested shall be placed in a bound volume with each item tabbed. When a number of sheets are required for an item, each sheet should be appropriately indexed, for example, Item 1(a), Sheet 2 of 6. Include with each response the name of the witness who will be responsible for responding to questions relating to the information provided. Careful attention shall be given to copied material to ensure its legibility. When the requested information has been previously provided in this proceeding in the requested format, reference may be made to the specific location of that information in responding to this request. When applicable, the requested information shall be provided for total company operations and jurisdictional operations, separately.

1. Explain why Dr. Vander Weide did not use the Capital Asset Pricing Model as one of his estimation tools to develop his cost of equity recommendation.

2. At page 4 of his Direct Testimony, Dr. Vander Weide states that his "recommended cost of equity is conservative because KAWC has significantly higher financial leverage, and, hence, greater financial risk, than my proxy companies." Provide the financial leverage for Kentucky-American and the proxy companies.

3. At page 9 of his Direct Testimony, Dr. Vander Weide discusses the relatively high degree of fixed costs that water utilities experience. To what other entities is Dr. Vander Weide comparing water utility fixed costs?

4. a. State Dr. Vander Weide's estimate of the price elasticity of demand for water within the United States.

b. State Dr. Vander Weide's estimate of the price elasticity of demand for water within Kentucky.

c. Provide all reports, studies, and other materials upon which Dr. Vander Weide relies to respond to Items 4(a) and 4(b).

5. Describe the effect of Kentucky-American's proposed Emergency Pricing Tariff, which is designed to recoup lost revenues during drought when water usage is curtailed, on the demand uncertainty that Kentucky-American experiences.

6. At page 10 of his Direct Testimony, Dr. Vander Weide discusses increasing costs related to meeting changing drinking water standards, replacing aging facilities and expanding existing facilities to meet growing demand. List and describe the options available to Kentucky-American to recover these costs.

7. At pages 13, 14, and 16 of his Direct Testimony, Dr. Vander Weide presents the equation for the Discounted Cash Flow ("DCF") model and describes *g* as

"the constant annual growth rate in earnings, dividends, and book value per share." He later states that he estimated the growth component in his DCF model, by using "the average analysts' estimates of future earnings per share (EPS) growth reported by I/B/E/S and the estimate of future earnings per share growth reported by Value Line." Explain why Dr. Vander Weide did not use growth in dividends and book value per share in his DCF model.

8. Provide the following materials to which Dr. Vander Weide refers in his testimony:

a. W. Carleton and J. Vander Weide, "Investor Growth Expectations and Stock Prices: the Analysts versus Historical Growth Extrapolation," *The Journal of Portfolio Management* (Spring 1988).

b. Lee Inmoo, Scott Lochhead, Jay Ritter, and Quanshui Zhao, "The Costs of Raising Capital," *The Journal of Financial Research*, Vol. XIX No 1 (Spring 1996).

c. Clifford W. Smith, "Alternative Methods for Raising Capital," *Journal of Financial Economics* 5 (1977).

d. Richard H. Pettway, "The Effects of New Equity Sales Upon Utility Share Prices," *Public Utilities Fortnightly*, (May 10, 1984).

9. Refer to the Direct Testimony of Dr. James H. Vander Weide at 19. Provide the stock price information from Standard & Poor's *Stock Guide* to which Dr. Vander Weide refers.

10. a. Dr. Vander Weide states that all firms that sell securities in the capital markets incur some level of flotation costs and estimates the flotation cost to RWE, Kentucky-American's parent, at approximately 5 percent of an equity issue.

Explain why, since the proceeds of most RWE equity issuances will not be invested in Kentucky-American, the entire flotation cost should be used to calculate Kentucky-American's cost of equity.

b. State whether in Dr. Vander Weide's opinion RWE is currently recovering any flotation costs from Kentucky-American.

c. Describe RWE's level of investment in Kentucky-American since the transfer of control of Kentucky-American to RWE.

d. List each RWE subsidiary that operates in the United States and that is a regulated public water utility, the state in which the subsidiary operates, the subsidiary's last return on equity ("ROE") award, the date of such award, and the amount or percentage of flotation cost used to calculate the subsidiary's cost of equity.

e. Describe RWE's current accounting treatment for flotation costs.

11. At page 26 of his Direct Testimony, Dr. Vander Weide testifies that he applied his DCF model to a proxy group of natural gas local distribution companies ("LDCs") that "are similar in risk to the water companies."

a. State whether, when comparing the risk of these LDCs to water companies, Dr. Vander Weide is referring only to the business risks factor that he discusses at pages 9 and 10 of his Direct Testimony.

b. Explain how the business risk factors discussed at pages 9 and 10 are similar for both water companies and LDCs.

c. List and describe the business risk factors that water companies face but LDCs do not.

d. List all reported decisions of which Dr. Vander Weide is aware in which a state regulatory commission accepted the use of natural gas LDCs as a proxy group for determining a water utility's cost of equity.

e. List all state regulatory proceedings in which Dr. Vander Weide testified and advocated the use of natural gas LDCs as a proxy group for determining a water utility's cost of equity.

12. a. State Dr. Vander Weide's estimate of the price elasticity of demand for natural gas within the United States.

b. State Dr. Vander Weide's estimate of the price elasticity of demand for gas within Kentucky.

c. Provide all reports, studies, and other materials upon which Dr. Vander Weide relies to respond to Items 12(a) and 12(b).

13. At page 30 of his Direct Testimony, Dr. Vander Weide states that "[p]revious studies have shown that the ex ante risk premium tends to vary inversely with the level of interest rates." State the reason(s), if any, that these studies provide for this inverse relationship.

14. Explain why Dr. Vander Weide used information from January 2004 to estimate the ex ante risk premium on an investment in Kentucky-American.

15. Provide a copy of page 75 of Ibbotson Associates' *2003 Yearbook*.

16. State whether Appendix 2 of Dr. Vander Weide's Direct Testimony has been published in a professional periodical or journal or has been submitted to a conference or other professional group. If it has been either published or submitted, provide the name of the publication or conference.

17. List all reported state utility regulatory commission decisions of which Dr. Vander Weide is aware in which a state utility regulatory commission treated flotation expenses as an additional element of a firm's cost of capital or allowed rate of return.

18. For each RWE subsidiary or affiliate that is a regulated water utility, identify each proceeding since January 1, 2002 in which the subsidiary or affiliate requested a rate adjustment, the regulatory commission in which the proceeding was conducted, the case number of the proceeding, and the date on which the proceeding was initiated.

19. Provide Kentucky-American's total water sales volume, by customer class, for each quarterly period since January 1, 1999. For each quarterly period, also provide a brief description of precipitation and temperature conditions.

20. Explain why Dr. Vander Weide did not include in his Direct Testimony a schedule similar to Schedule C that included his proxy water companies.

21. State whether RWE has access to and uses financial markets outside of the United States when it issues debt instruments or equity.

22. Describe how RWE raises its capital and allocates this capital to its subsidiaries and affiliates.

23. Describe the process under which Kentucky-American would obtain capital investment from RWE for new capital expenditures.

24. State the conditions under which a subsidiary or affiliate of RWE may publicly issue its own debt or equity to persons or entities not related to RWE or RWE affiliates.

25. List each debt and equity issuance that RWE has made since January 1, 2001. For each issuance listed, state the date of the issuance, its purpose and the

extent to which the proceeds of the issuance were used for the acquisition of the assets of or control of another entity.

26. At pages 65 and 66 of his Direct Testimony, Michael M. Miller states that the 25 percent reduction in rates for low-income customers should be recovered by spreading "the cost of the discount across all customer classes."

a. Identify the benefits, if any, that other customers receive as a result of Low Cost Customer Tariff.

b. Explain why requiring other customers to assume the cost of the discount is fair and reasonable.

c. State whether, if the cost of the discount is spread across all customer classes, low-income customers will be allocated a portion of the cost of the discount.

27. a. State the amount of funds from the "Water for Life Fund" that were distributed to customers or used to reduce customer bills in 2003.

b. State the number of customers that benefited from the "Water for Life Fund" in 2003 in the form of reduced bill or billing credit and the total amount of bill reduction or credit.

c. List each use that Kentucky-American made of the "Water for Life Fund" in 2003.

d. Describe how Kentucky-American identifies customers who were to receive reduced bills or billing credits from the "Water for Life Fund." Provide all written policies and operating procedures for the fund.

28. Explain how, in the absence of any express statutory authority to provide a separate customer classification based upon a customer's income, the Commission may authorize the "Low Income Customer Tariff" assistance for low-income customers.

29. a. List each American Water Works Company affiliate or subsidiary that has established a Low Income Tariff or similar program.

b. For each entity listed above,

(1) Provide a copy of the tariff and all policies or operating procedures for the operation of the tariff.

(2) Describe the results of the entity's tariff. Provide all reports, audits, or regulatory commission reviews of the entity's tariff.

30. List each American Water Works Company affiliate or subsidiary that has established a voluntary assistance or contribution program and describe the results of that program. The description should include the level of monies collected in 2003 and a discussion of the efforts to publicize and promote such program.

31. State Kentucky-American's position on any condition to the implementation of the Low Income Tariff that requires Kentucky-American to assume a share of the cost of the discount equal to that borne by Kentucky-American ratepayers.

32. Describe Kentucky-American's proposed method of allocating the cost of discount resulting from its proposed Economic Development Tariff among its remaining customers and its shareholders.

33. Identify each American Water Works Company subsidiary that assesses an activation fee, provide a copy of its tariff sheet setting forth such fee, and describe how the fee is calculated.

34. List all non-American Water Works Company water utilities of which Coleman Bush is aware that assess an activation fee.

35. State whether a customer may be assessed both an Activation Fee and a Reconnection Fee when service is reconnected or restored.

36. Refer to the Direct Testimony of Coleman D. Bush, Exhibit 2. For miscellaneous expense allocated to direct service order labor, describe how the allocation was made.

37. At page 15 of his Direct Testimony, Mr. Bush refers to a "dramatic increase in costs including enhanced communication and community education and more frequent meter readings" resulting from a drought emergency. Describe what Mr. Bush means by "dramatic increase in costs."

38. Refer to Direct Testimony of Coleman D. Bush at 15. State how frequently, in Mr. Bush's opinion, formal meetings with the Commission would have to be held while the Emergency Pricing Tariff is in effect.

39. Refer to the Direct Testimony of Linda C. Bridwell at 29.

a. Describe the bidding process through which Kentucky-American selects contractors.

b. Describe the qualifications that a contractor must meet to be eligible to participate in the bidding process.

c. Provide a copy of the most recent request for bids that Kentucky-American issued to contractors.

d. State the number of contractors that Kentucky-American awarded with contracts to make new tap installations for each year since January 1, 2000.

e. Describe how, if Kentucky-American has more than 1 contractor performing service tap installations, a contractor is assigned to perform a service tap installation.

f. State whether Kentucky-American conducts separate bid solicitations for its Central and Northern Divisions.

g. State whether different contractors are used for Kentucky-American's Central and Northern Divisions.

40. State why Kentucky-American bases its tap fees on a 3-year average cost of the installation of new services.

41. State why, if a single contractor performs all installations of new services, tap fees are not based upon current costs as opposed to an average cost.

42. Refer to the Direct Testimony of Linda C. Bridwell at 30.

a. Explain why Kentucky-American's labor costs have increased due to more stringent verification of the accuracy of work and tracking of materials.

b. Explain why Kentucky-American's assumption of additional duties previously held by contractors would not result in lower contract labor costs and offset at least a portion of Kentucky-American's increased labor costs.

c. Identify the cost savings achieved as a result of Kentucky-American's assumption of responsibility for purchasing and tracking materials from contractors.

d. Describe "the insurance issues following September 11, 2001" to which Ms. Bridwell refers and how these issues have affected the cost of service installations.

43. Identify who (i.e., Kentucky-American employee or contractor) performs service connection installations for Kentucky-American's Northern Division.

44. Explain why Kentucky-American is proposing the same tap fee for 1-inch and 2-inch services for both Divisions, but proposes different fees for each division for 5/8-inch services and larger size services.

45. Refer to Kentucky-American's Application, Exhibit 3 at 3. Explain why Kentucky-American's proposed tap fee for 1-inch and 2-inch services for Northern Division-Elk Lake is listed in its Notice as "Actual Cost" but is listed in Ms. Bridwell's Direct Testimony as $945 and $4,250, respectively.

46. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 9-1 at 1. The column labeled "2004 Meter" lists $45 for 5/8-inch meter, $82 for 1-inch meter, and $299 for 2-inch meter. Explain how these amounts were established.

47. Refer to Direct Testimony of Dr. Edward L. Spitznagel at 2. State the number of companies screened in Dr. Spitznagel's model that are <u>not</u> subsidiaries of American Water Works Company.

48. Identify the other variables that Dr. Spitznagel considered in his model in addition to those identified at Page 4 of his Direct Testimony.

49. Refer to Direct Testimony of Dr. Edward L. Spitznagel at 4.

a. Describe how Dr. Spitznagel's projections of residential and commercial customer daily utilization in this proceeding compare to those in previous proceedings before this Commission.

b. Describe the developing trends in average daily utilization, if any, that Dr. Spitznagel finds from his modeling.

c. State the implications of these developing trends, if any, on Kentucky-American's costs of production and revenues from water sales.

50. Refer to the Direct Testimony of James E. Salser at 8-10. For each customer class in which Mr. Salser has made changes to reflect an increase in customers due to normal growth, provide the assumptions used to calculate the number of additional customers, show the calculations used to derive the change, and explain the reasoning for the change.

51. Refer to Kentucky-American's Application, Exhibit 37, Schedule M. Provide a copy of this schedule in Excel® 97 spreadsheet format.

52. Provide a schedule that lists, by name and title, each of the 133 Kentucky-American employees included in the forecasted test period. Provide on the schedule, separately, the amounts forecasted to be paid to or on behalf of each individual for regular time and overtime, incentive pay plan, 401 K plan and any other labor expense included in forecasted labor costs. Then, show the forecasted allocation or direct assignment of payroll costs to each business unit of Kentucky-American for the forecasted test period. Then, detail on this schedule, the accounts to which each of those amounts are forecasted to be recorded (e.g., capital plant accounts, labor expense accounts, deferred asset accounts for security costs, condemnation case, other system acquisitions). This schedule shall include totals for all amounts listed. The schedule should include but not be limited to total forecasted labor of $5,140,435, $158,820, and $44,408 for Central Division, Tri Village, and Elk Lake, respectively, in full detail.

53. Provide a schedule containing the information requested in Item 52 for all persons that Kentucky-American employed during the calendar year ending December 31, 2003.

54. Explain how Kentucky-American, when developing a forecasted test period, determines the appropriate accounting treatment (e.g., expensing, capitalizing, deferring as a regulatory asset) the forecasted payroll costs for an employee.

55. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-8. Kentucky-American employee Linda Bridwell assisted in the preparation and filing of Kentucky-American's application for rate adjustment.

a. State what portion, if any, of the historical labor costs attributable to her, that is included in regulatory expense listed.

b. If no historical labor costs attributable to Ms. Bridwell are included in regulatory expenses, explain why none were included.

c. If historical labor costs attributable to Ms. Bridwell are included in regulatory expenses, explain how Kentucky-American accounted for this occurrence when determining the cost of her labor for forecasted test period expenses.

56. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-1. For each of the vacant personnel positions listed in forecasted labor costs, state:

a. The reason(s) why the position must be filled.

b. The reason(s) why the position is currently vacant.

c. The current status of Kentucky-American's efforts to fill the position.

d. The total cost of the position included in the forecasted test period (i.e. payroll expenses, payroll capitalized, retirement, taxes, insurance benefits) and the accounts to which each amount was charged.

57. For Kentucky-American's forecasted incentive pay program:

a. List all Kentucky-American employees who are eligible to participate in the program.

b. State the level of incentive pay available to each participant in the forecasted period.

c. State the level of incentive pay awarded to all individuals participating in the program for the previous 5 years compared to level of incentive pay available to each participant in the forecasted period.

d. Explain how incentive payment awards in previous years were determined.

e. State the amounts of incentive payment awards included in the forecasted test period.

f. Explain how the amounts of incentive payment awards included in the forecasted test period were determined.

58. Refer to the Direct Testimony of Coleman D. Bush at 8. Only 10 percent of Barbara Brown's and David Whitehouse's labor and other expenses are allocated to Kentucky-American because their involvement to the source of supply issue and condemnation proceeding that Lexington–Fayette Urban County Government ("LFUCG") has brought allow them "almost no time available to devote to Kentucky American Water's other businesses." Explain why, as Roy Mundy has been directed by Kentucky-American's Board of Directors to "devote his full time and energies to

defending the Company" against the same condemnation proceeding,[1] the same ratemaking treatment has not been proposed for Mr. Mundy's labor and other expense.

59. Refer to the Direct Testimony of Michael M. Miller at 27, lines 2-3. Identify all expenses related to the LFUCG condemnation proceeding that Kentucky-American has included in the forecasted test period rate base and expenses.

60. In Exhibit 1 of his Direct Testimony, Coleman Bush details the allocation of costs common to Kentucky-American's regulated and non-regulated business units.

a. Explain how this allocation is reflected in Exhibit 37, Schedule C2, of Kentucky-American's Application.

b. Show the detailed calculations used to derive each component of the total Labor Direct and Common costs allocated of $1,227,364.

61. Refer to the Direct Testimony of Michael M. Miller at 62-63. Mr. Miller testifies that to avoid "rate shock" Kentucky-American proposes to allocate only one-third of the identifiable costs to its Northern Division districts.

a. State the effect on the Northern Division's proposed rates if all identified costs are allocated to the Northern Division District. Provide all workpapers, state all assumptions, and show all calculations used to identify the rate impact.

b. Explain why the allocation of the Northern Division's costs to the Central Division is fair and reasonable to the Central Division's customers.

c. Explain why Kentucky-American did not propose a uniform tariff for all customers in this proceeding rather than announce its intention to seek such a tariff in its next rate case proceeding.

[1] Direct Testimony of Chris E. Jarrett at 5 - 6.

d. Describe the effect on Kentucky-American's proposed rates if a uniform tariff for both divisions were used in this proceeding. Provide all workpapers, state all assumptions, and show all calculations used to calculate the effects of a uniform tariff.

62. a. State whether any of the field employees listed in the 133 forecasted personnel positions provide services to Kentucky-American's non-regulated operations.

b. For each field employee who provides services to Kentucky-American's non-regulated operations, describe how the employee's time is assigned or allocated to those operations.

63. Provide, using the same format as found in Kentucky-American's Application, Exhibit 37, Schedule C-2, a fully disclosed forecasted income statement that details separately revenues and expenses of all non-regulated activities and calculation of net income.

64. List, for each of Kentucky–American's 5 most recent applications for rate adjustments, the amount of rate case expense incurred and state whether Kentucky-American used a historical test period or future test period in its application.

65. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-8. State whether, in Kentucky-American's opinion, the stated rate case expense of $622,409 would be less if the application was based upon an historical test period. Explain.

66. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-8. State the amount of the rate case

expense of $622,409 that may be attributed to the budgeting process necessary to develop the forecasted test period.

67. a. State and quantify the benefits to Kentucky-American ratepayers from Kentucky-American's use of a forecasted test period in this case and all previous forecasted test period rate cases. State all assumptions and show all calculations used to derive the quantification of benefits.

b. State and quantify the benefits to Kentucky-American shareholders from Kentucky-American's use of a forecasted test period in this case and all previous forecasted test period rate cases. State all assumptions and show all calculations used to derive the quantification of benefits.

68. Describe the actions that Kentucky-American has taken to ensure that the most cost effective and economical approaches to rate application filings are used.

69. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-8 at 1. Provide for each component of "Cost of preparation and presentation of current case":

a. The names of the persons providing services and a description of those services.

b. The hourly rate charged by each person.

c. The initial budgeted time of each individual to complete the application process.

d. The actual time and amounts billed by each individual to date.

e. The amount of time estimated to finish the rate application process by each individual.

70. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-8 at 2. Provide for each individual listed:

a. The complete name of the individual providing the service(s) and a description of those services.

b. The hourly rate charged.

c. The initial budgeted time to complete the application process.

d. The individual's actual time and amounts billed to date.

e. The individual's estimate of the amount of time to complete his or her portion of the rate application process.

71. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-8 at 2.

a. Explain the category "Shared Services."

b. Provide a detailed analysis of the amount reported as "Shared Services."

c. Explain how the Overhead ratio of 1.56 was calculated, state all assumptions, and show the calculations.

72. Explain why Kentucky-American proposes a 3-year amortization period for rate case expenses.

73. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-8

a. State when Kentucky-American last contracted out to independent consultants the services listed in Workpapers 3-8.

b. Provide for each services listed in Workpapers 3-8 that were provided by independent consultants Kentucky-American's request for proposals and all bids received in response.

74. a. Provide a current organizational chart for American Water Works Company ("AWWC") that includes all subsidiaries and service companies and depicts how each relate to another as far as services and functions provided.

b. Describe how AWWC's subsidiaries and service companies determine charges and billings for each service or function provided.

75. State whether AWWC is currently undertaking a restructuring process with the ultimate goal of reducing its workforce.

76. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 1-12 at 2.

a. Provide a detailed analysis of the amounts accrued by Kentucky – American totaling $629,839.84 for the Customer Care Center in Alton, Illinois.

b. Provide a detailed calculation of the Customer Case Center amortization expense of $8,900.

c. Provide a detailed analysis of the amounts accrued by Kentucky – American totaling $704,179.34 for the National Shared Services Center in Morlton, New Jersey.

d. Provide a detailed calculation of the National Shared Services Center amortization expense of $13,417.

77. At page 23 of his Direct Testimony, Michael M. Miller testifies regarding the deferral of costs related to the Customer Care Center and National Shared Services Center that "I have also reviewed rate filings and Orders of all other American Water

regulated subsidiaries and know of no other jurisdiction that has denied similar prudently incurred and cost justified expenditures for rate recovery." Provide a copy of the Orders to which Mr. Miller refers.

78. Refer to the Direct Testimony of Michael M. Miller, Exhibit MAM-5 at 3 and 5. Provide the account numbers for the listed expense accounts where savings are shown and describe how the amounts were determined. Show all calculations and state all assumptions used to determined the amount of savings.

79. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 4-1 at 7.

a. Reconcile the amount shown as amortization of $703,518 to the expense at Kentucky-American's Application, Exhibit 37, Schedule C-2, page 1, of $695,154.

b. Explain the entry "Pinville Acq."

c. Explain why the amortization expense for Boonesboro is stated at $1,104 monthly while it appears as $1,087.57 at Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 1-12, Page 1.

80. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-5 and the Direct Testimony of Coleman D. Bush, Exhibit 1. Provide a reconciliation of the management fees listed on the two schedules.

81. State whether any of Kentucky-American's non-regulated business units receives services from any of the related parties whose charges to Kentucky-American

are included in management fees. If yes, describe the service(s) received and how their costs are allocated or assigned to those non-regulated activities.

82. a. Provide a detailed analysis of the amounts recorded as acquisition adjustments for Tri-Village Water District and Elk Lake.

c. For each acquisition, demonstrate that:

(1) The purchase price was established through arms-length negotiations.

(2) The Initial investment plus the cost of restoring the facilities to required standards will not adversely impact the overall costs and rates of Kentucky-American's existing and new customers.

(3) Operational economies were achieved through the acquisition.

(4) The purchase price of utility and non-utility property can be clearly identified.

(5) The purchase will result in overall benefits in the financial and service aspects of Kentucky-American's operations.

83. Identify the proceedings in which the Public Service Commission of Kentucky allowed rate base treatment for unamortized rate case expenses as Kentucky-American requests.

84. Identify the pertinent sections of the Orders of the Public Service Commission of Kentucky in which approval of rate base treatment for the Deferred Legal Settlement Costs addressed in Case Number 2000-00120[2] was granted.

[2] Case No. 2000-00120, Adjustment of the Rates of Kentucky-American Water Company (Ky. PSC).

85. Refer to the Direct Testimony of Dr. Kenneth I. Rubin's at 15.

a. Identify the three locations that Kentucky-American secured with Lexington off-duty police officers.

b. State whether the locations listed in Item 86(a) were the same locations that Alliance Staffing secured?

c. Identify all other locations that Alliance Staffing personnel secured?

d. Describe the actions that Kentucky-American took to replace Alliance Staffing personnel and services when its contract with Alliance Staffing ended on August 19, 2003.

e. Provide the amounts, expense accounts charged, and vendor providing the security services at these three or any other locations as included in the forecasted test period.

86. Refer to the Direct Testimony of Michael M. Miller at 30, Line 7.

a. Provide a detailed analysis of the $143,194 included in forecasted test year expenses for "on-going security expenses."

b. Provide the expense accounts and amounts charged during the forecasted test period for "on-going security expenses."

c. List all capital costs related to "Security Costs" that are included in forecasted test year depreciation expense.

d. State whether all related capital costs have been accrued to Security Costs – Deferred Debit.

87. Refer to the Direct Testimony of Dr. Kenneth I. Rubin at 16, Lines 5-11.

a. List all sources in addition to Jackie Howard on which Dr. Rubin relies for the proposition that "65-70 percent overhead for temporary W-2 employees is common in the industry and covers the cost of scheduling, management, liability insurance, statutory benefits, and a 10-15 percent profit."

b. Describe the research that Dr. Rubin has conducted to support the proposition that "65-70 percent overhead for temporary W-2 employees is common in the industry and covers the cost of scheduling, management, liability insurance, statutory benefits, and a 10-15 percent profit."

c. List all sources on which Dr. Rubin relies for the proposition that "in the professional services industry, of which consulting is a part, this level of overhead [65-70 percent] is considered reasonable."

d. Provide the estimates or bid solicitation responses that Kentucky-American received from other providers for the services that Alliance Staffing provided from April 1, 2002 to August 19, 2003. If Kentucky-American did not receive any estimates or bid solicitation responses, then explain why.

88. Refer to the Direct Testimony of Dr. Kenneth I. Rubin at KR Schedule 2.

a. Provide the estimated useful life of the assets listed as Items 1 through 6 and 8 through 12.

b. Provide a detailed analysis and description of the costs included as Item 7, Security Office Building, in the amount of $7,445.26.

c. List the costs, if any, that are included on KR Schedule 2 and reflected in the forecasted test period depreciation expense. For each listed cost, state its original costs and the amount of annual depreciation expense included in the forecasted test year.

89. Refer to the Direct Testimony of Dr. Kenneth I. Rubin at KR Schedule 3.

a. Provide a detailed analysis and description of the costs included as Item 7, Security Office Building, in the amount of $10,257.18.

b. Provide the estimated useful life of the assets listed as Items 8 through 37, 43, 46 through 49, and 53 through 59.

c. State whether "Porta Potty Rental," Item 41, is an annual recurring expense that is included in the forecasted test year.

d. Provide a detailed analysis and description of the costs included as Item 42, "Securing Tanks," in the amount of $152,581.

e. Provide a detailed analysis and description of the costs included as Item 44, "Clearing Fence Lines," in the amount of $6,230.55. Explain how this activity differs from routine fence clearing.

f. Provide a detailed analysis and description of costs included as Item 45, KAW Labor, in the amount of $4,436.70.

g. Provide a detailed analysis and description of the costs included as Item 50, "Survey work at Tank Sites," in the amount of $9,300.

h. Provide a detailed analysis and description of the costs included as Item 52, "Communications Equip., Fees, and Misc.," in the amount of $194,665.41.

i. Identify the costs included on KR Schedule 3, if any, that are reflected in the forecasted test period depreciation expense. For each identified cost, state its original costs, and the amount of annual depreciation expense included in the forecasted test year.

90. Refer to the Direct Testimony of Dr. Kenneth I. Rubin at KR Schedules 2 and 3.

a. Included on Schedule 2 are “Pre 9/11” costs of security systems at the [**Confidential Materials Omitted**]. Identify the Security System costs listed on Schedule 3 for each of those locations, if any, were incurred to supplement or replace the system’s costs included on Schedule 2. Explain.

b. Identify any assets or costs listed on these schedules that have been taken out of service or will be taken out of service prior to the end of the forecasted test period.

91. Reconcile the amounts included in KR Schedules 2 and 3 of Dr. Rubin’s Direct Testimony to the total Security Costs of $2,805,661.79 as shown at Kentucky-American’s Response to Commission Staff’s First Set of Information Requests, Item 1(a), Workpapers 1-12, Page 2.

92. State the amount included in the forecasted test period for community education efforts toward conservation. State the expense account titles and numbers where this amount was recorded.

93. Refer to the Direct Testimony of Michael M. Miller at 48, lines 3-4. Identify the utilities whose incentive plans are in line with that of Kentucky-American and provide a copy or summary of each utility’s incentive plan.

94. Provide copies of any studies or analysis that Kentucky-American has performed that quantifies the benefits that the customers have received from the Incentive Plan.

95. Refer to the Direct Testimony of Sheila A. Valentine at 6, lines 19-20. Provide detailed workpapers supporting the calculation of forecasted purchased water based on 2003 actual usage and appropriate costs.

96. Refer to the Direct Testimony of Sheila A. Valentine at 6, lines 27-30. Provide detailed workpapers supporting the calculation of forecasted system delivery of 14,463 million gallons based on the 5-year monthly history of pumpage and adjustments.

97. Refer to the Direct Testimony of Sheila A. Valentine at 6-7. Describe each adjustment that was made to the historical pumpage information that was based upon "judgment concerning future events."

98. Refer to the Direct Testimony of Sheila A. Valentine at 7, Lines 8-16.

a. List those chemicals where operational judgment was used in the development of the forecast. Explain how operational judgment was used in the development of the forecast. Show all calculations and state all assumptions used in the development of these forecasts.

b. Provide the basis for the forecasted general price increase of 2.5 percent.

c. Provide for each chemical listed in Workpapers 3-3 a 5-year analysis of the price changes that have occurred over the 5 years prior to the rate application filing.

99. Refer to the Direct Testimony of Sheila A. Valentine at 7 and Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-4.

a. Provide all bids for the forecasted cleaning of KRS and RRS.

b. State whether the forecasted cleaning of RRS is an annual expense. If it is not an annual expense, explain why Kentucky-American did not propose to amortize the forecasted amount.

c. State when cleaning of each station included in the forecasted amount will be completed.

d. Provide detailed workpapers supporting the monthly recurring expense of $3,500 for each station.

100. Refer to the Direct Testimony of Sheila A. Valentine at 7 - 8.

a. State for each of the seven vacant positions listed in Workpapers 3-1 the amount included in Group Insurance.

b. Provide documentary evidence in the form of invoices or other statements of the 8.94 percent increase that is scheduled to become effective January 1, 2005.

c. Provide the OPEB analysis prepared by Towers Perrin to which Ms. Valentine refers. Also provide all workpapers resulting in an annual expense of $809,063. Include detailed workpapers that include all actuarial assumptions.

d. Explain why OPEB costs are not included in Workpapers 3-6?

e. At Kentucky-American's Application, Exhibit 37, Schedule C-2, page 1, the amount included as forecasted Group Insurance is $1,724,407. The amounts included in Ms. Valentine's testimony for OPEB's and in Workpapers 3-6 for insurance are $809,063 and 937,643, respectively, for a total expense of $1,746,706. Reconcile the amount included in Schedule C-2 with those included in Ms. Valentine's testimony and Workpapers 3-6.

f. (1) Provide the most recent historical actuarial study for OPEB's performed for Kentucky-American.

(2) Provide the workpapers for the most recent historical actuarial study.

(3) List all actuarial assumptions of this study.

(4) List and explain any differences in the actuarial assumptions in this study from those used in Towers Perrin's OPEB analysis.

101. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-6. Provide all workpapers, show all calculations, and state all assumptions used to derive the capitalization rate of 19.53 percent.

102. Provide all studies and analyses that Kentucky-American has performed since the conclusion of Case No. 2000-00120 regarding the reasonableness and cost-effectiveness of its 1989 Service Company contract.

103. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpaper 3-5 and Item 34. Provide a reconciliation of the management fees for the forecasted period contained on these schedules.

104. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-7 at 2.

a. Provide the actuarial study supporting the schedule at this page.

b. Provide all workpapers, show all calculations and state all assumptions used in the actuarial study.

105. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-10 at 1-2. Provide for each listed expense account a detailed description of the items included in the account. State all assumptions used in developing the budgeted amounts for the forecasted test period and explain why such assumptions are reasonable. Explain and illustrate the relationship between the forecasted amount and a historical period where applicable.

106. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-11 at 1. Provide for each listed expense account a detailed description of the items included in the account. State all assumptions used in developing the budgeted amounts for the forecasted test period and explain why such assumptions are reasonable. Explain and illustrate the relationship between the forecasted amount and a historical period where applicable.

107. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-12 at 1-3. Provide for each listed expense account a detailed description of the items included in the account. State all assumptions used in developing the budgeted amounts for the forecasted test period and explain why such assumptions are reasonable. Explain and illustrate the relationship between the forecasted amount and a historical period where applicable.

108. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 3-13 at 1-2. Provide for each listed expense account a detailed description of the items included in the account. State all assumptions used in developing the budgeted amounts for the forecasted test period and explain why such assumptions are reasonable. Explain and illustrate the relationship between the forecasted amount and a historical period where applicable.

109. Refer to Kentucky-American’s Response to Commission Staff’s First Set of Information Requests, Item 1(a), Workpapers 3-14 at 1. Provide for each listed expense account a detailed description of the items included in the account. State all assumptions used in developing the budgeted amounts for the forecasted test period and explain why such assumptions are reasonable. Explain and illustrate the relationship between the forecasted amount and a historical period where applicable.

110. Identify all costs related to the future retirement of assets included in rate base that were accrued by Kentucky-American pursuant to Statement of Financial Accounting Standard 143 “Accounting for Asset Retirement Obligations.”

111. Provide for each category set forth below a detailed listing of the amounts included in the forecasted operating expenses (above the line) by title and the account number used in the Uniform System of Accounts for Class A and B Water Companies:

a. Social and Service Club Dues.

b. Charitable Contributions.

c. Initiation/Country Club Expenses.

d. Employee Party, Outing and Gift Expenses.

e. Spousal Travel

f. Sales Promotion and Advertising

g. Civic, Political, and Related Activities

h. Employee Bonuses Outside of the Incentive Plans

112. Provide a comparison of Kentucky-American’s forecasted rate base, capital structure, and income statement from Case No. 2000-00120 with its actual results. Provide for each variance a detailed explanation for the variance.

113. Provide a monthly comparison of Kentucky-American's forecasted construction expenditures from Case No. 2001-00120 with its actual results by construction project. Provide for each variance a detailed explanation for the variance.

114. a. List each construction project that will be commenced and/or completed during the forecasted test period for which Kentucky-American, as of the date of this Request, has not obtained all necessary governmental permits, licenses, or other approvals.

b. For each project,

(1) List all required governmental permits, licenses, or other approvals.

(2) List those governmental permits, licenses, or other approvals Kentucky-American has not obtained as of the date of this Order.

(3) State the date Kentucky-American applied or expects to apply for such governmental permit, license, or other approval.

115. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 10. The 10-year average ratio of actual to budgeted capital construction ("slippage factors") for the Investment Projects B-H is 105.43 percent and 86.12 percent for the Investment Projects. Recalculate Kentucky-American's forecasted revenue requirement, rate base, and cost-of-service study as follows:

a. Adjust all monthly Investment Projects B-H expenditures beginning February 2004 through the end of the forecasted test period, using the 105.43 slippage factor.

b. Reduce all monthly Investment Projects expenditures beginning February 2004 through the end of the forecasted test period, using the 86.12 slippage factor.

c. Provide all workpapers, assumptions, and calculations showing the effect of the slippage factors to each forecasted element of rate base, and cost-of-service study.

116. For each investment project started and/or completed during the period 1994 through 2003, provide:

a. The number of investment projects that were completed ahead of schedule.

b. The number of investment projects that were completed on schedule.

c. The number of investment projects that were completed behind schedule.

117. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 10 at 1. Investment Projects 92-12, 96-19, 89-01, 98-08, 89-09 were originally scheduled for completion prior to 2003 but were not completed on schedule. Explain why, although $840,868 was expended on these projects during 2003, no funds were budgeted in 2003 for these projects.

118. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), Workpapers 1-11. Provide for the deferred maintenance projects listed below the date on which the project was completed, a description of the project, and the basis for the amortization period:

a. Work Order No. 1105, Paint Tates Creek.

b. Work Order No. 1106, Sadieville Standpipe Repairs.

c. Work Order No. 50030635, Cox Street Tank Repairs.

d. Work Order No. 50030636, Tri-Village Paint Long Ridge Tank.

119. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 8. State when, if ever, Kentucky-American plans to undertake a new Least Cost/Comprehensive Planning Study such as it conducted in 1992.

120. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 9. For each of the budgeted projects listed below, provide a detailed description of the project and the basis for the budgeted amounts.

a. Source of Supply Project.

b. Source of Supply Project – Consortium.

121. Refer to the Direct Testimony of James E. Salser at 3.

a. Explain why 12 months of data was analyzed for the expenses while only 91 days was used for the revenues.

b. Explain why 2002 data was used to analyze revenues.

122. Refer to the Direct Testimony of Michael M. Miller at 6-8.

a. As of March 1, 2004, Kentucky-American has issued $38 million of its authorized long-term debt of $41.5 million, but it intends to issue an additional $5.5 million of long-term debt in the forecasted test-period. State whether Kentucky-American intends to request Commission approval before issuing the $5.5 million of new debt.

b. State whether Kentucky-American issued any common stock when issuing the $38 million of long-term debt. If Kentucky-American issued common stock, describe the issuance.

123. At Exhibit 17, page 3, of its Application, Kentucky-American predicts that its equity-to-capital ratio will exceed 45 percent in calendar years 2005 and 2006. State and describe the actions that Kentucky-American intends to take to maintain equity-to-capital ratio between 35 to 45 percent as the Public Service Commission of Kentucky directed in Case No. 2002-00317.[3]

Robert A. Amato for

Beth O'Donnell
Executive Director
Public Service Commission
P. O. Box 615
Frankfort, Kentucky 40602

DATED: June 14, 2004

cc: Parties of Record

[3] See Case No. 2002-00317, The Joint Petition of Kentucky-American Water Company, Thames Water Aqua Holdings GmbH, RWE Aktiensgelschaft, Thames Aqua Holdings, Inc., Apollo Acquisition Company and American Water Works Company, Inc. for Approval of a Change of Control of Kentucky-American Water Company (Ky. PSC Dec. 20, 1002), Appendix A at 4.