

**COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION**

**IN THE MATTER OF:** )  
 )  
**NOTICE OF ADJUSTMENT OF THE RATES OF** ) **CASE NO. 2008-00427**  
**KENTUCKY-AMERICAN WATER COMPANY** )  
**EFFECTIVE ON AND AFTER NOVEMBER 30, 2008** )

**APPLICATION, STATEMENT AND NOTICE**

Comes Kentucky-American Water Company and states as follows:

1. Kentucky-American Water Company (“Kentucky American Water”) is a corporation organized and existing under the laws of the Commonwealth of Kentucky with its principal office, place of business and post office address at 2300 Richmond Road, in Lexington, Fayette County, Kentucky.

2. Kentucky American Water is a wholly-owned subsidiary of American Water Works Company, Inc. (“American Water”) and is engaged in the distribution and sale of water in its Central Division, consisting of Bourbon, Clark, Fayette, Harrison, Jessamine, Scott and Woodford Counties and its Northern Division, consisting of Gallatin, Owen and Grant Counties. It currently owns, operates and maintains potable water production, treatment, storage, transmission and distribution systems for the purpose of furnishing potable water for residential, commercial, industrial and governmental users in its service territory.

3. To meet continuing demand for adequate service, Kentucky American Water has been and will continue to be required to expend money to renovate its existing facilities, improve and enlarge its facilities, construct new facilities, and to reinforce and extend its distribution system through the end of the forecasted test year in this proceeding. The increase in the cost of service and the additional capital expenditures have not been offset by the additional income

produced by the increase in rates effective December 1, 2007 in Case No. 2007-00143 with the result of an erosion of earnings of Kentucky American Water as reflected in the attached exhibits. An increase in its rates is essential for Kentucky American Water to maintain a reasonable level of service, to meet the expanding needs of its service area and to have a reasonable opportunity for appropriate earnings. An increase is also essential for Kentucky American Water's customers to avoid the rate shock that would result if the recovery of construction expenses associated with the Kentucky River Station II project is delayed until after that project is completed. Kentucky American Water must have income to sufficiently and properly provide for all expenses of an efficient public utility, market its securities, attract replacement capital for maturing debt and to attract new capital, all at reasonable costs. The rates presently charged by Kentucky American Water are insufficient to meet its requirements because they no longer are compensatory and are, therefore, unfair, unreasonable and unjust.

4. As authorized by KRS 278.192(1) and for the purpose of justifying the reasonableness of the proposed increase in rates, Kentucky American Water has utilized a forward-looking test period corresponding to the first twelve (12) consecutive calendar months the proposed rates will be in effect after the six-month suspension of the proposed rates. The forward-looking test period is the twelve months ending May 31, 2010.

5. Kentucky American Water has used, in the attached exhibits, a base period consisting of the twelve (12) months ending January 31, 2009. This base period begins not more than nine (9) months prior to the date of the filing of this Application, and is a period consisting of not less than six (6) months of historical data and not more than six (6) months of estimated data, all as authorized by KRS 278.192(2)(a).

6. Within forty-five (45) days after the last day of the base period, Kentucky American Water will file the actual results for the estimated months of the base period as required by KRS 278.192(2)(b).

7. Kentucky American Water's annual reports, including the annual report for 2007, are on file with the Public Service Commission as required by 807 KAR 5:006, Section 3(1).

8. Kentucky American Water gives notice to the Public Service Commission of the adjustment of its rates from those set forth in Exhibit No. 1 in the filing requirements to those rates set forth in Exhibit No. 2 in the filing requirements, in the total amount of \$18,494,634 on an annual basis. The percentage of increase will approximate an overall increase of 31.27% to Kentucky American Water. A comparison of the current and proposed rates is set forth in attached Exhibit No. 3.

In Case No. 2007-00143, the Commission approved the implementation of single-tariff pricing for Kentucky American Water. Accordingly, the rates for each customer class are and will be uniform throughout each customer class without regard to which Kentucky American Water division a customer is in. The estimated amount of increase per customer class in both dollars and as a percentage is: residential, \$9,249,890, 30.24%; commercial, \$5,229,196, 34.73%; industrial, \$647,870, 39.91%; municipal or private fire connections, \$316,634, 39.01%; public fire hydrants, \$650,586, 26.38%; private fire hydrants, \$172,535, 39.01%; municipal and other public authority, \$1,696,872, 37.65%; and, sales for resale, \$531,038, 38.91%

The effect upon the average bill for each customer class that the proposed rate change will apply is an increase in the following dollar and percentage amounts: residential, \$7.02, 30.60%; commercial, \$46.32, 35.35%; industrial, \$1,241.87, 39.83%; municipal or private fire connections, \$23.52, 39.04%; public fire hydrants, \$85.92, 26.38%; private fire hydrants,

\$211.44, 39.01%; municipal and other public authority, \$200.74, 37.25%; and sales for resale, \$2,117.94, 39.52%.

9. Kentucky American Water is a corporation, and a certified copy of its Articles of Incorporation, together with all amendments, are incorporated by reference as authorized by 807 KAR 5:001, Section 10(1)(b)3 and Section 8(3), and were filed as Filing Exhibit No. 4 in Case No. 95-554, Notice of the Adjustment of The Rates of Kentucky American Water Company Effective on and after February 29, 1996, and are referred to in the attached Exhibit No. 4.

10. Kentucky American Water is a corporation in good standing with the Secretary of State of the Commonwealth of Kentucky. A certificate to that effect, dated within sixty (60) days of October 31, 2008, as required by 807 KAR 5:001, Section 10(1)(b)5, is attached as Exhibit No. 5.

11. The legal name of the applicant is Kentucky-American Water Company. It does business under an assumed name and has filed a Certificate of Assumed Name as required by KRS 365.015. A certified copy of the Certificate of Assumed Name as required by 807 KAR 5:001, Section 10(1)(b)6 is attached as Exhibit No. 6.

12. Kentucky American Water has complied with 807 KAR 5:011, Section 8(2) and 807 KAR 5:001, Section 10(3) and (4), by mailing a typewritten Customer Notice to all customers no later than the date this Application, Statement and Notice was filed with the Public Service Commission and by posting a sample copy of the Customer Notice at its principal office and place of business in each division no later than the date this Application, Statement and Notice was filed with the Public Service Commission. A copy of the Customer Notice is attached as Exhibit No. 7.

13. Kentucky American Water has filed with the Executive Director of the Public Service Commission a written notice of its intention to file this rate application. The notice stated that the application would be supported by a fully forecasted test period, was delivered to the Executive Director's office on September 30, 2008, and a copy was provided to the Utility Intervention and Rate Division of the Attorney General's office of the Commonwealth of Kentucky as required by 807 KAR 5:001, Section 10(2) and 807 KAR 5:011, Section 8(1). A copy of the notice is attached as Exhibit No. 8.

14. As required by 807 KAR 5:001, Section 10(4)(f), Kentucky American Water will post a copy of Exhibit No. 7 of the filing requirements at its places of business on October 31, 2008, and it will remain posted until the Public Service Commission has finally determined Kentucky American Water's rates.

15. In support of its application for a general adjustment of rates, supported by a fully forecasted test year, Kentucky American Water has presented its financial data for the forecasted period in the form of pro forma adjustments to the base period, has limited the forecasted adjustments to the twelve (12) calendar months immediately following the suspension period, and has based capitalization and net investment rate base on a thirteen (13) month average for the forecasted period, all as set forth in 807 KAR 5:001, Section 10(8)(a)(b) and (c), in Exhibits No. 37B, 37D and 37J.

16. In further support of its application for a general adjustment of rates, supported by a fully forecasted test year, Kentucky American Water attaches the following documents or explains their absence:

<b>Filing Requirements</b>	<b>Abbreviated Document Description</b>	<b>Location or Absence Reason</b>
807 KAR 5:001 Section 10(8)(f)	Rate base/capital reconciliation	Exhibit 9
807 KAR 5:001 Section 10(9)(a)	Testimony of Witnesses - Patrick Baryenbruch - Linda C. Bridwell - Keith Cartier - Nick O. Rowe - Paul Herbert - Michael A. Miller - Dr. Edward L. Spitznagel, Jr. - Sheila Miller - Dr. James H. Vander Weide	Exhibit 10
807 KAR 5:001 Section 10(9)(b)	Capital construction budget with a 3-year forecast	Exhibit 11
807 KAR 5:001 Section 10(9)(c)	Description of forecast factors	Exhibit 12
807 KAR 5:001 Section 10(9)(d)	Annual and monthly budget for 12 months preceding 10/31/08, the base period and the forecasted period	Exhibit 13
807 KAR 5:001 Section 10(9)(e)	Nick O. Rowe's statement of attestation	Exhibit 14
807 KAR 5:001 Section 10(9)(f)	Information about major construction projects	Exhibit 15
807 KAR 5:001 Section 10(9)(g)	Information about other construction projects	Exhibit 16
807 KAR 5:001 Section 10(9)(h)1	Financial forecast for the capital construction forecasted years - operating income statement	Exhibit 17

807 KAR 5:001 Section 10(9)(h)2	Financial forecast for the capital construction forecasted years - balance sheet	Exhibit 18
807 KAR 5:001 Section 10(9)(h)3	Financial forecast for the capital construction forecasted years - cash flow statement	Exhibit 19
807 KAR 5:001 Section 10(9)(h)4	Financial forecast for the capital construction forecasted years - revenue requirements	Exhibit 20
807 KAR 5:001 Section 10(9)(h)5	Financial forecast - energy and demand load forecast	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(h)6	Financial forecast - access line forecast	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(h)7	Financial forecast - generation mix	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(h)8	Financial forecast - gas supply mix	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(h)9	Financial forecast for the capital construction forecasted years - employee level	Exhibit 21
807 KAR 5:001 Section 10(9)(h)10	Financial forecast for the capital construction forecasted years - labor cost changes	Exhibit 22
807 KAR 5:001 Section 10(9)(h)11	Financial forecast for the capital construction forecasted years - capital structure requirements	Exhibit 23
807 KAR 5:001 Section 10(9)(h)12	Financial forecast for the capital construction forecasted years - rate base	Exhibit 24
807 KAR 5:001 Section 10(9)(h)13	Financial forecast for the capital construction forecasted years - water sales (gallons)	Exhibit 25

807 KAR 5:001 Section 10(9)(h)14	Financial forecast for the capital construction forecasted years - customer forecast	Exhibit 26
807 KAR 5:001 Section 10(9)(h)15	Financial forecast - gas sales forecast	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(h)16	Financial forecast - toll and access forecast	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(i)	FERC or FCC audit reports	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(j)	Most recent stock or bond prospectus	Exhibit 27
807 KAR 5:001 Section 10(9)(k)	FERC 1, FERC 2, ARMISR and PSCT	Inapplicable to a water company
807 KAR 5:001 Section 10(9)(l)	Annual reports to shareholders, most recent five years	Exhibit 28
807 KAR 5:001 Section 10(9)(m)	Current chart of accounts	Exhibit 29
807 KAR 5:001 Section 10(9)(n)	Latest 12 monthly managerial reports	Exhibit 30
807 KAR 5:001 Section 10(9)(o)	Monthly budget variance reports for 12 months pre-base period, for base period, and subsequent months as available	Exhibit 31
807 KAR 5:001 Section 10(9)(p)	SEC 10-Ks, 8-Ks and 10-Qs	Not required of Kentucky American Water
807 KAR 5:001 Section 10(9)(q)	Independent auditor's annual opinion report and any written findings of material weaknesses in internal controls	Exhibit 32  There is no finding of material weaknesses.
807 KAR 5:001 Section 10(9)(r)	Quarterly reports to shareholders	Kentucky American Water does not issue quarterly reports to shareholders.
807 KAR 5:001 Section 10(9)(s)	Summary of last depreciation study	Exhibit 33
807 KAR 5:001 Section 10(9)(t)	List of software, programs and models used	Exhibit 34

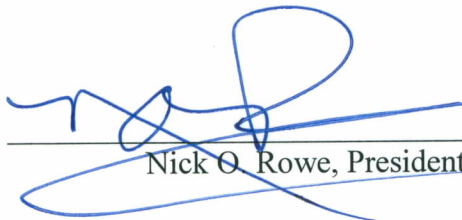


807 KAR 5:001 Section 10(9)(u)	Affiliate, general or home office allocations	Exhibit 35
807 KAR 5:001 Section 10(9)(v)	Cost of service study	Exhibit 36
807 KAR 5:001 Section 10(9)(w)	Cost of service study for local exchange carriers	Inapplicable to a water company
807 KAR 5:001 Section 10(10)(a)	Jurisdictional financial summary for the base and forecasted period	Exhibit 37, Schedule A
807 KAR 5:001 Section 10(10)(b)	Jurisdictional rate base summary for the base and forecasted period	Exhibit 37, Schedule B
807 KAR 5:001 Section 10(10)(c)	Jurisdictional operating income summary for base and forecasted period	Exhibit 37, Schedule C
807 KAR 5:001 Section 10(10)(d)	Jurisdictional adjustment to operating income	Exhibit 37, Schedule D
807 KAR 5:001 Section 10(10)(e)	Jurisdictional federal and state income tax summary for base and forecasted period	Exhibit 37, Schedule E
807 KAR 5:001 Section 10(10)(f)	Organizational membership dues, initiation fees, country club expenditures, charitable contributions, marketing expenses, sales expenses, advertising expenses, professional service expenses, civic and political activity expenses, employee parties and outings expenses, employee gift expenses, and rate case expenses for the base and forecasted periods	Exhibit 37, Schedule F
807 KAR 5:001 Section 10(10)(g)	Payroll costs analysis	Exhibit 37, Schedule G
807 KAR 5:001 Section 10(10)(h)	Computation of gross revenue conversation factor	Exhibit 37, Schedule H
807 KAR 5:001 Section 10(10)(i)	Comparative income statements, revenue statistics and sales statistics for five most recent calendar years, the base period, forecasted period and two calendar years beyond the forecast period	Exhibit 37, Schedule I
807 KAR 5:001 Section 10(10)(j)	Cost of capital summary for base period and forecasted period	Exhibit 37, Schedule J

807 KAR 5:001 Section 10(10)(k)	Comparative financial data and earning measures for the ten most recent calendar years, base period and forecasted period	Exhibit 37, Schedule K
807 KAR 5:001 Section 10(10)(l)	Narrative description and explanation of all proposed tariff changes	Exhibit 37, Schedule L
807 KAR 5:001 Section 10(10)(m)	Revenue summary for base period and forecasted period with detailed billing analysis for all customer classes	Exhibit 37, Schedule M
807 KAR 5:001 Section 10(10)(n)	Typical bill comparison under present and proposed rates for all customer classes	Exhibit 37, Schedule N

This Application, Statement and Notice is filed under the provisions of KRS 278.180 and 278.190, and the Commission is requested to find the proposed rates to be fair, just and reasonable under KRS 278.030(1).

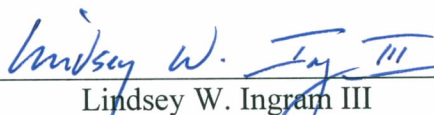
KENTUCKY-AMERICAN WATER COMPANY

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