

DAMON R. TALLEY, P.S.C.

112 N. LINCOLN BLVD.
P.O. BOX 150
HODGENVILLE, KENTUCKY 42748

TEL. (270) 358-3187
FAX (270) 358-9560

DAMON R. TALLEY

ATTORNEY AT LAW

March 20, 2008

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

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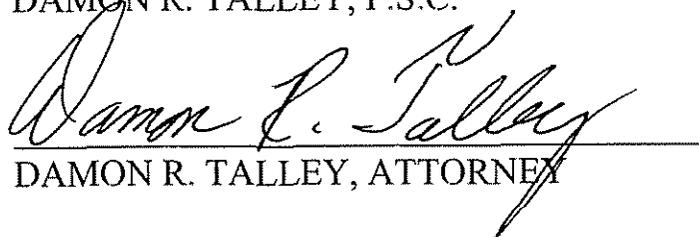
PUBLIC SERVICE
COMMISSION

RE: Case No. 2007-00134
Kentucky-American Water Company

Dear Ms. O'Donnell:

Enclosed for filing are the original and ten (10) copies of the Bluegrass Water Supply Commission's Post-Hearing Brief.

Yours truly,
DAMON R. TALLEY, P.S.C.


DAMON R. TALLEY, ATTORNEY

DRT/ms

Enclosures

cc: All Parties of Record

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF KENTUCKY-AMERICAN)
 WATER COMPANY FOR A CERTIFICATE OF)
 CONVENIENCE AND NECESSITY)
 AUTHORIZING THE CONSTRUCTION OF) CASE No. 2007-00134
 KENTUCKY RIVER STATION II, ASSOCIATED)
 FACILITIES AND TRANSMISSION MAIN)
)

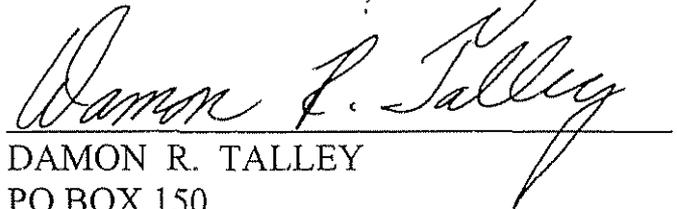
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MAR 20 2008

PUBLIC SERVICE
COMMISSION

POST - HEARING BRIEF
OF
BLUEGRASS WATER SUPPLY COMMISSION

Respectfully submitted,
 DAMON R. TALLEY, P.S.C.



DAMON R. TALLEY
 PO BOX 150
 112 N. LINCOLN BLVD.
 HODGENVILLE, KY 42748
 (270) 358-3187 FAX (270) 358-9560
 ATTORNEY FOR BLUEGRASS WATER
 SUPPLY COMMISSION

INTRODUCTION

This case is before the Commission on the application of Kentucky-American Water Company (“KAWC”) for a Certificate of Public Convenience and Necessity (“CPCN”) authorizing the construction of certain water supply, treatment and transmission facilities. The facilities are described in KAWC’s application, but, for purposes of this Brief, are summarized as follows: (1) raw water intake and water treatment plant on Pool 3 of the Kentucky River; (2) approximately 30 miles of a 42-inch diameter transmission main; (3) booster pump station; and (4) water storage tank (the “Facilities” or the “Pool 3 Project”). The total estimated cost of the Facilities is approximately \$160 million.

KAWC’s application was filed on March 30, 2007. Thereafter, pursuant to a procedural schedule established by the Commission, exhaustive discovery occurred.

The Commission conducted an evidentiary hearing on November 26, 27 and 28, 2007 (the “November Hearing”) and a supplemental evidentiary hearing on March 5 and 6, 2008 (the “March Hearing”).

This Brief is being filed on behalf of Bluegrass Water Supply Commission (“BWSC”) pursuant to the schedule established in the Commission’s February 27, 2008 Order. It addresses not only the usual and customary CPCN issues but also those issues enumerated in Appendix E to the Commission’s Order of December 21, 2007.

ISSUES PRESENTED

- I. WHETHER THERE IS A NEED FOR THE FACILITIES?
- II. WHETHER CONSTRUCTION OF THE FACILITIES WILL RESULT IN WASTEFUL DUPLICATION OF FACILITIES?
- III. WHETHER THE LOUISVILLE WATER COMPANY ("LWC") HAS THE LEGAL AUTHORITY TO MAKE WHOLESALE WATER SALES IN THE COUNTIES OTHER THAN JEFFERSON COUNTY AND THOSE COUNTIES THAT ARE CONTIGUOUS TO JEFFERSON COUNTY?
- IV. WHETHER THE LWC HAS THE STATUTORY AUTHORITY TO CONSTRUCT, OWN AND OPERATE A WATER TRANSMISSION MAIN IN COUNTIES OTHER THAN JEFFERSON COUNTY AND THOSE COUNTIES THAT ARE CONTIGUOUS TO JEFFERSON COUNTY FOR THE PURPOSE OF MAKING WHOLESALE WATER SALES IN COUNTIES OTHER THAN JEFFERSON COUNTY AND THOSE COUNTIES THAT ARE CONTIGUOUS TO JEFFERSON COUNTY?
- V. WHETHER THE LEXINGTON - FAYETTE URBAN COUNTY GOVERNMENT ("LFUCG") HAS THE STATUTORY AUTHORITY TO CONSTRUCT, OWN AND OPERATE A JOINT PUBLIC-PRIVATE VENTURE TO SUPPLY WATER TO KAWC AND ANY OTHER REGIONAL WATER SUPPLIERS?
- VI. WHETHER THE COMMISSION, AS A CONDITION FOR GRANTING A CPCN FOR THE PROPOSED FACILITIES, MAY LIMIT THE AMOUNT THAT KAWC MAY INCLUDE IN ITS RATE BASE FOR RATE-MAKING PURPOSES TO THE ESTIMATED COST OF THE PROPOSED FACILITIES AT THE TIME A CPCN IS ISSUED?

ARGUMENT

KAWC cannot commence constructing the Facilities until it obtains a “certificate that public convenience and necessity require the service or construction” pursuant to KRS 278.020(1). This statute is silent on what standards the Commission should use in determining whether to issue a CPCN. Not surprisingly, a large body of case law has developed to fill this void. The leading and most cited Kentucky case is Kentucky Utilities Company v. Public Service Commission, 252 S.W.2d 885 (Ky. 1952) in which the Court stated:

Therefore, a determination of public convenience and necessity requires both a finding of the need for a new service system or facility from the standpoint of service requirements, and an absence of wasteful duplication resulting from the construction of the new system or facility. *Id.* at 890.

Thus, there are two (2) issues for the Commission to decide: (1) whether the Facilities are **needed**; and (2) whether the construction will result in a **wasteful duplication of facilities**.

I.

THE COMMISSION HAS PREVIOUSLY DETERMINED AND KAWC HAS DEMONSTRATED THE NEED FOR THE FACILITIES.

The water supply shortage in central Kentucky and the water treatment plant capacity deficit of KAWC have been publicly debated and reported in the Lexington Herald-Leader for two (2) decades. As a result, almost everyone,

including those University of Kentucky football fans who visit Lexington in the fall and those out-of-town racing fans who attend Keeneland's spring or fall meets and peruse a copy of the Lexington Herald-Leader, can attest to the water supply shortage in central Kentucky and the treatment plant capacity deficit of KAWC.

Not only is the public aware of these water shortage issues, but the Commission has also been aware of them for at least 15 years. In 1993, the Commission initiated an investigation into the sources of supply and future demand of KAWC¹. At the conclusion of that investigation, the Commission determined that a substantial water supply deficit would exist during an extreme drought situation.² In addition, the Commission placed the responsibility of developing "an adequate and reliable source of water supply" for KAWC's customers squarely upon the shoulders of KAWC.³

In the last paragraph of its August 21, 1997 Order in Case No. 93-434, the Commission stated:

IT IS THEREFORE ORDERED that Kentucky-American shall take the necessary and appropriate measures to obtain sources of supply so that the quantity and quality of water delivered to its distribution system shall be sufficient to adequately, dependably, and safely supply the total reasonable

¹ Case No. 93-434, An Investigation of the Sources of Supply and Future Demand of Kentucky-American Water Company.

² Case No. 93-434, Order of August 21, 1997, p. 5.

³ *Id.*, p.6.

requirements of its customers under maximum consumption through the year 2020.⁴

Thereafter, KAWC successfully negotiated a Water Supply Agreement with LWC.⁵ Significant, organized opposition to the proposed Louisville pipeline arose. In 1999, a severe drought struck central Kentucky and the entire Kentucky River Watershed. Public awareness of the substantial water supply shortage was heightened. KAWC's customers experienced water use restrictions imposed by LFUCG for four (4) months.⁶ LFUCG adopted its infamous 1999 Resolution favoring a Kentucky River solution to the water supply problem and supporting regional cooperation.⁷ The Louisville pipeline proposal then experienced a slow death.

The 1999 drought also spawned the creation of the Bluegrass Water Supply Consortium ("Consortium") and, ultimately, BWSC to address the regional water supply shortage in central Kentucky and to seek a regional solution. The Consortium, working in cooperation with the Bluegrass Area Development District, engaged the services of O'Brien and Gere Engineers, Inc. ("O'Brien & Gere") and undertook a comprehensive regional study of the water supply needs of central Kentucky.

⁴ *Id.*

⁵ See LWC November Hearing Exhibit 5.

⁶ Bridwell Direct Testimony, pp. 12-13.

⁷ *Id.*, Exhibit A.

Meanwhile, in 2001, the Commission initiated another investigation into KAWC's water supply deficit.⁸ During the course of that proceeding, the 2004 Water System Regionalization Feasibility Study (the "Regional Study" or the "O'Brien & Gere Report") was prepared and filed with the Commission.⁹ The Regional Study estimated that KAWC's water supply deficit would be 29.8 MGD in 2020.¹⁰ Additional evidence was compiled that further demonstrated both the immediacy and the magnitude of KAWC's water supply shortage and treatment plant capacity deficit. The Commission has incorporated all records from Case No. 93-434 and Case No. 2001-00117 into the record of this case.¹¹

Ms. Linda Bridwell, in her Direct Testimony filed with the Application in this case, summarizes the magnitude of the water supply shortage during drought conditions and the treatment plant capacity deficit.¹² Tables 1 and 2 of her Direct Testimony also illustrate the immediacy of the shortage. If a severe drought occurs in 2010, then KAWC customers will face a raw water shortage of 20 MGD. The shortage is projected to be 25 MGD in 2020 and grows to 28 MGD in 2030. This testimony is not disputed.

⁸ Case No. 2001-00117, An Investigation into the Feasibility of Kentucky-American Water Company's Proposed Solution to its Water Supply Deficit.

⁹ The Regional Study was filed on June 28, 2004 in Case No. 2001-00117.

¹⁰ See Written Comments of BWSC filed on March 31, 2005 in Case No. 2001-00117

¹¹ PSC Case 2007-00134, Commission Order of August 1, 2007.

¹² Bridwell Direct Testimony, pp. 29-30.

Table 2 of Ms. Bridwell's Direct Testimony also demonstrates that KAWC will have a treatment plant capacity deficit of over 10 MGD in 2010. That treatment plant capacity deficit is projected to reach over 21 MGD by 2030.

In summary, the overwhelming need for the Facilities to eliminate the raw water shortage and the treatment plant capacity deficit of KAWC is "crying out" from the boxes of reports, studies, written testimony, exhibits, the Transcript of Evidence and other materials that have been amassed in Case No. 93-434, Case No. 2001-00117 and this case. KAWC has easily demonstrated the need for the Facilities.

II.
**THE POOL 3 PROJECT IS A REASONABLE
SOLUTION AND WILL NOT RESULT IN WASTEFUL
DUPLICATION OF FACILITIES.**

The second prong of the test set forth in the 1952 Kentucky Utilities case¹³ is whether the proposed construction will result in a wasteful duplication of facilities. On the surface, this evaluation is easy. Is there an existing 36-inch or 42-inch diameter water transmission main capable of delivering an additional 20 or 25 MGD of potable water to Lexington and Fayette County? Is there such a transmission main running parallel to I-75? Does such a transmission main exist along the I-64 corridor? Does such a transmission main traverse Fayette County in another location? The answer to all these questions is, "No."

¹³ Kentucky Utilities Company v. Public Service Commission, 252 S.W.2d 885 (Ky. 1952) at 890.

Therefore, KAWC must build a transmission main from Lexington to a reliable source of water. The construction of such a line will not duplicate any existing facilities. Hence, there can be no “wasteful” duplication.

Public policy demands that the Commission probe deeper. The next step in this analysis is to evaluate whether the Kentucky River Pool 3 Project proposed by KAWC is a reasonable and feasible solution to its water supply and treatment plant deficit problems. Logically, the Commission should ask, “Have there been any independent studies conducted?” If so, “What solutions did those studies recommend?” Fortunately, such a study exists.

The most comprehensive, independent study concerning the water supply alternatives for central Kentucky is the Regional Study prepared by O’Brien & Gere. It was published in 2004 and filed with the Commission.¹⁴ The Regional Study recommended that a large regional water treatment plant be constructed adjacent to Pool 3 of the Kentucky River.

The Regional Study was prepared by O’Brien and Gere for the Bluegrass Area Development District in association with the Consortium.¹⁵ The Regional Study has been discussed at length throughout this proceeding and has been identified by various names including: the “O’Brien and Gere Report”; the “O’Brien and Gere Study”; the “Regional Feasibility Study”; and, perhaps, by other

¹⁴ The Regional Study was filed on June 28, 2004 in Case No. 2001-00117.

¹⁵ The Consortium was the predecessor organization of BWSC.

names. The report shall be referred to as the “Regional Study” throughout the remainder of this Brief.

The Regional Study commenced in August 2002 and was completed in February 2004. It identified and evaluated 40 unique water supply alternatives for central Kentucky, including purchasing treated water from LWC.

The O’Brien & Gere Consultant Team recommended the Kentucky River Pool No. 3 alternative based on its highest overall score. On October 13, 2003 at Workshop No. 6, the Consortium members voted unanimously to accept the recommendation of the Consultant Team and selected the Kentucky River Pool 3 alternative as the best alternative for solving the water supply deficit in central Kentucky.¹⁶

During the conduct of the Regional Study, both O’Brien & Gere and the Consortium members considered and rejected two (2) proposals from LWC.¹⁷ Following the publication of the Regional Study, LWC submitted Proposal No. 3 and Proposal No. 4 to BWSC. Once again, these proposals were evaluated and rejected by BWSC in favor of the Pool 3 solution.¹⁸

The record in this case contains not only the Regional Study by O’Brien & Gere but also the Water Supply Study performed by the engineering firm of

¹⁶ See BWSC Responses to Commission’s Post-Hearing Information Requests, Item 1 for a more thorough discussion of the alternatives considered and the evaluation process.

¹⁷ *Id.* @ Item 1, p. 6 of 11.

¹⁸ *Id.* @ Item 1, pp. 6-8 of 11.

Gannett Fleming (the “Gannett Fleming Study”) at the request of KAWC.¹⁹ In 2005, KAWC engaged the services of Gannett Fleming to review and evaluate existing reports (including the Regional Study prepared by O’Brien & Gere), to provide an updated cost comparison of the previously identified top alternatives (including both the Pool 3 solution and the LWC pipeline), and to review KAWC’s deficits and demand projections. Gannett Fleming issued its Study in March 2007. Gannett Fleming determined that the Pool 3 Project was feasible, less expensive than the LWC pipeline, and was the best alternative for KAWC to pursue. In making this determination, Gannett Fleming validated the Pool 3 solution first identified by O’Brien & Gere and first proposed by BWSC.

Late one night while preparing this Brief and after having looked through box after box of documents for a certain report, this attorney realized that the report he was seeking does not exist. He thought his search had been in vain. He thought his efforts were futile. In reality, his “discovery” that the report did not exist was golden. He “discovered” there is an immense “hole” in the evidence. There is **no engineering report** in the record **challenging** the feasibility of the Pool 3 Project!

The Regional Study prepared by O’Brien & Gere and the Gannett Fleming Study both conclude that the Pool 3 solution is the best solution for solving the raw water shortage and the treatment plant capacity deficit of KAWC. There is no

¹⁹ KAWC Responses to Commission Staff’s First Set of Interrogatories, Item 6

contradictory engineering report in the record questioning the feasibility or reasonableness of the scope of the Pool 3 Project.²⁰ The lack of such an engineering report “speaks” volumes.

It is patently unfair to compare the “known and measurable” costs of the Pool 3 Project to the speculative cost assumptions for the Louisville to Lexington pipeline concept(s) being promoted by LWC. Nevertheless, the magnitude of the capital and operating costs associated with both the Pool 3 Project and the LWC pipeline concept(s), the long-lasting impact the Commission’s decision will have upon hundreds of thousands of citizens and ratepayers, and other considerations demand that such a comparison be made using the best information currently available. Suffice it to say, neither alternative will be cheap.

To make matters more difficult, the Pool 3 Project will require a significantly higher initial capital investment than the LWC pipeline concept(s). On the other hand, the annual operating costs of the Pool 3 Project will be significantly less than the operating costs associated with the LWC pipeline concept(s). Thus, it is difficult to make an “apples to apples” comparison.

As expected, each side has experts and the experts disagree. KAWC’s expert has testified that the present worth of the Pool 3 Project will be less than that of the LWC pipeline concept(s). LWC’s expert has testified that the present worth of the

²⁰ T.E. November Hearing, Volume III, p. 332, lines 1-2 where Dr. Wetzel admits the Beck Report is a financial comparison and not an “engineering report.”

LWC's pipeline concept(s) will be less than that of the Pool 3 Project. Each expert uses different assumptions to support his findings.

Scott Rubin, the expert for the Office of the Attorney General ("OAG"), stands alone from the other experts. In his Rebuttal Testimony dated November 13, 2007, Mr. Rubin testified that "the costs of the project proposed by KAWC are **reasonably close** to the only other option identified (the LWC pipeline and water purchase)."²¹ (Emphasis added). In other words, it is a "wash" or a "toss-up."

Mr. Rubin also testified about the sensitivity of the LWC option to the amount of water purchased. A much greater percentage of the costs associated with the LWC option vary with the amount of water purchased. In contrast, the incremental cost of producing an additional 1,000 gallons of water from the Pool 3 treatment plant is relatively small because most of the costs are fixed rather than variable costs. Thus, if the combined KAWC and BWSC water demand increases by only 1.25 MGD each year, then the Pool 3 Project becomes the more cost effective option.²² As the combined water usage increases above this "tipping point," the more cost effective the Pool 3 Project becomes.

The pricing structure proposed by LWC is another factor which weighs heavily against purchasing water from LWC. In order to receive LWC's most "favorable" rate of \$1.71 per 1,000 gallons at the Shelbyville delivery point,

²¹ Rubin Rebuttal Testimony, p. 10, Line 7.

²² *Id.*, p. 9.

KAWC's and BWSC's peak day purchases may not exceed two (2) times the minimum daily purchase.²³ The minimum purchase amount specified by LWC is 5 MGD. Assume that KAWC and BWSC contract to purchase a combined minimum amount of 5 MGD. In this example, the combined purchases of KAWC and BWSC cannot exceed 10 MGD (5 MGD x 2). If they exceed this amount, then an additional demand charge will be added to the \$1.71 rate for the following 24 months.

Assume that KAWC and BWSC contract with LWC to reserve **pipeline** capacity of 25 MGD. Under LWC's reserve capacity ratio of 2:1, then KAWC and BWSC must purchase a minimum of 12.5 MGD (25 MGD ÷ 2). The cost of purchasing 12.5 MGD per day each and every day for the next 20 years at the **current** rate of \$1.71 exceeds **\$156 million** (12.5 MGD x \$1.71 x 365 x 20).

The reasonableness of the Pool 3 Project becomes more apparent when it is contrasted with the various pipeline concepts promoted by LWC. First, consider the evolution of the Pool 3 Project. An independent engineering firm (O'Brien & Gere) identified Pool 3 as an adequate and reliable source of water for solving the region's water supply needs. Another engineering firm, Gannett Fleming, later independently reached the same result. Since then, KAWC has done the following: (1) obtained options to purchase the property for the raw water intake, water

²³ Heitzman October 1, 2007 Rebuttal Testimony, p. 6.

treatment plant, booster pump station, and storage tank sites; (2) selected a route for the transmission main; (3) designed all the facilities; (4) performed all the necessary environmental studies; (5) obtained all the necessary permits, except for the CPCN; (6) secured the necessary financing; (7) advertised and received bids to construct the Facilities; (8) secured time extensions from the successful bidders; and (9) taken all other necessary preparatory actions prior to commencement of construction.

KAWC has successfully moved the Pool 3 Project from the idea stage to the concept stage, to the proposal stage, to the project stage, to the planning stage, to the design stage, to the approval stage and is now ready to commence construction pending the Commission's approval of the CPCN.

In stark contrast is LWC's lack of progress. Despite having made numerous "presentations" concerning a Louisville to Shelbyville to (insert the name of your city) pipeline during the past few years, LWC's desire to sell treated water to central Kentucky has been frustrated. In fairness, LWC's idea for constructing a pipeline to central Kentucky initially advanced from the idea stage to the concept stage. It mutated, however, into multiple concepts after having been scrutinized by the public, by elected officials and by the rigorous review process of the Commission. LCW's desire to sell water to central Kentucky will never come to fruition until, and unless, some entity steps forward and makes the financial commitment to construct the pipeline segment from Shelbyville to Lexington.

LWC had such a partner in 1998 when it signed the Water Supply Agreement with KAWC. It lost that partner in 1999. Despite ongoing efforts to obtain another partner during the last nine (9) years, it has been unsuccessful. The lack of a partner is a **fatal flaw**. The Commission has given LWC opportunity after opportunity after opportunity to correct this flaw. LWC has been unable to do so.

The urgent need for solving central Kentucky's water supply shortage and KAWC's treatment plant deficit prevents the Commission from waiting any longer for some viable entity to volunteer to become the owner of a Shelbyville to Lexington pipeline. KAWC's request for a CPCN should be granted without any further delay.

III.
**LWC DOES NOT HAVE THE LEGAL AUTHORITY
TO WHOLESALE WATER TO COUNTIES OTHER
THAN JEFFERSON COUNTY AND THOSE
COUNTIES ADJOINING JEFFERSON COUNTY.**

The relevant statute is KRS 96.265 which states:

The board of waterworks may extend the waterwork corporation's facilities to **provide water service to persons within and outside the city of the first class, including extensions into counties adjoining its county of origin**. In extending service to persons not presently served within the city and county of the waterwork corporation's origin it may, but is not required to, make water line extensions recovering the cost thereof, KRS 96.539 notwithstanding, by assessment as provided in this section. (Emphasis added). (Subsections (1) through (11) of KRS 96.265 pertaining to assessments have been omitted).

KRS 96.265 was enacted by the legislature in 1988. Its purpose was twofold: (1) to define the service area of LWC as Jefferson County and all counties adjacent to Jefferson County; and (2) to establish a statutory mechanism for LWC to recover the cost of extending waterlines to unserved areas of Jefferson County by assessing the benefited property owners. KRS 96.265 does not differentiate between “retail” and “wholesale” water service. The statute simply refers to “water service”. Therefore, a plain reading of the statute prohibits LWC from providing water service of any type, either “retail” or “wholesale”, beyond its territorial limits. The territorial limits of LWC include Jefferson County and all counties adjacent to Jefferson County.

**IV.
LWC DOES NOT HAVE THE STATUTORY
AUTHORITY TO CONSTRUCT, OWN AND
OPERATE A WATER TRANSMISSION MAIN IN
COUNTIES OTHER THAN JEFFERSON COUNTY
AND THOSE COUNTIES ADJOINING JEFFERSON
COUNTY.**

KRS 96.265 prohibits LWC from extending its “facilities to provide water service” beyond Jefferson County and those counties adjoining Jefferson County. LWC is governed by KRS 96.230 to 96.310. KRS 96.265, however, is the only statute which addresses the territorial boundaries or service area of LWC. After diligent research, this attorney cannot find any case law interpreting KRS 96.265.

Therefore, the plain meaning of this statute is controlling. LWC cannot legally construct, own, nor operate a water transmission main in Franklin, Woodford, Scott, Fayette nor any other county along the I-64 corridor east of Shelby County. Presumably, this is why LWC has consistently stated that its delivery point will be in **Shelby County** at the Kentucky Highway 53 exit.

V.

LFUCG DOES NOT APPEAR TO HAVE THE STATUTORY AUTHORITY TO CONSTRUCT, OWN AND OPERATE A JOINT PUBLIC-PRIVATE VENTURE TO SUPPLY WATER TO KAWC AND ANY OTHER REGIONAL WATER SUPPLIERS.

This attorney is a novice to the body of law concerning the powers and limitations of LFUCG. The LFUCG Charter and KRS Chapter 67A pertaining to urban-county governments are complex. Consequently, a general practitioner, such as this attorney, will be “skating on thin ice,” if he tries to render a definitive, legal opinion to this question posed by the Commission. Nevertheless, there are at least two (2) statutes that prevent LFUCG from entering into a joint public-private venture with KAWC to supply water to KAWC and other regional water suppliers.

First, LFUCG is an urban-county government created by charter. Both its charter and KRS 67A.070 limit LFUCG’s activities to its “territorial limits”; i.e., Fayette County. Thus, it would appear that LFUCG cannot construct or acquire waterworks facilities outside Fayette County. If it cannot own facilities outside

Fayette County, then it cannot enter into a joint venture to own facilities outside Fayette County.

Second, since LFUCG does not currently own a water supply system, KRS 96.150 is also a legal obstacle preventing LFUCG from constructing or acquiring waterworks facilities outside Fayette County. KRS 67A.060 empowers LFUCG with all “the constitutional and statutory rights, powers, privileges, immunities and responsibilities” of a city of the second class.²⁴ As such, LFUCG can avail itself of all the provisions of Chapter 96 applicable to second class cities. KRS 96.150 permits second class cities to own or construct waterworks outside its corporate limits if, and only if, the city already owns a water supply system. LFUCG does not own a water supply system. Thus, KRS 96.150 is a second legal hurdle preventing LFUCG from participating in a joint venture to own facilities outside Fayette County.

VI.
THE COMMISSION, AS A CONDITION FOR GRANTING A CPCN FOR THE PROPOSED FACILITIES, MAY NOT LIMIT THE AMOUNT THAT KAWC MAY INCLUDE IN ITS RATE BASE FOR RATE-MAKING PURPOSES TO THE ESTIMATED COST OF THE PROPOSED FACILITIES AT THE TIME A CPCN IS ISSUED.

There is no statutory authority for the Commission to impose any such conditions upon the issuance of a CPCN. A certificate case is controlled by KRS

²⁴ Lexington was a city of the second class before the creation of LFUCG.

278.020(1), which does not permit the Commission to impose conditions upon its issuance of a CPCN.

In contrast, however, is KRS 278.020(6), which **expressly** authorizes the Commission to impose conditions in a transfer of ownership or change of control case. KRS 278.020(6) provides:

The commission may make investigation and hold hearings in the matter as it deems necessary, and thereafter may grant any application under this subsection in whole or in part and with modification and **upon terms and conditions as it deems necessary or appropriate**. The commission shall grant, modify, refuse, or **prescribe appropriate terms and conditions** with respect to every such application . . . (Emphasis added).

Thus, the Commission has the legal authority to grant conditional approval in a transfer of ownership case under KRS 278.020(6). It **lacks** the authority, however, to issue a conditional CPCN under KRS 278.020(1).

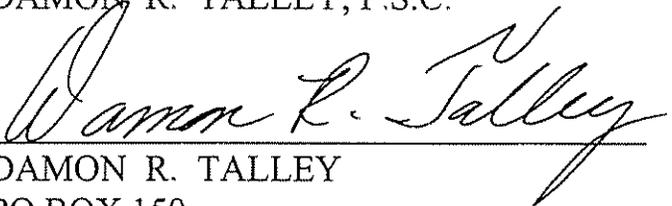
The Commission's granting of a CPCN for KAWC to construct the Facilities will not, however, diminish the Commission's rate-making role. KAWC will not get an automatic "pass" when it comes before the Commission for a rate increase. KAWC will not be, and should not be, guaranteed automatic rate recovery for the Facilities simply because the Commission issues a CPCN.

CONCLUSION

For the foregoing reasons, the Commission should grant KAWC a CPCN to construct the Facilities. In addition, the CPCN should contain the flexibility for KAWC to construct a 25 MGD water treatment plant rather than a 20 MGD treatment plant in the event BWSC exercises one of the options contained in the November 20, 2007 Agreement between BWSC and KAWC.

This 20th day of March, 2008.

Respectfully submitted,
DAMON R. TALLEY, P.S.C.



DAMON R. TALLEY
PO BOX 150
112 N. LINCOLN BLVD.
HODGENVILLE, KY 42748
(270) 358-3187 FAX (270) 358-9560
ATTORNEY FOR BLUEGRASS WATER
SUPPLY COMMISSION

CERTIFICATE OF SERVICE

This is to certify that a true copy of the foregoing document has been served by first class U.S. Mail, postage prepaid, this 20th day of March, 2008, to the following:

Hon. A. W. Turner, Jr., Gen. Counsel
Kentucky –American Water Co.
2300 Richmond Road
Lexington, Kentucky 40502

Hon. Lindsey W. Ingram, III
Stoll Keenon Ogden PLLC
300 West Vine Street, Suite 2100
Lexington, Kentucky 40507-1801

Hon. David E. Spenard
Assistant Attorney General
1024 Capital Center Drive, Suite 200
Frankfort, KY 40601-8204

Hon. David J. Barberie
Lexington-Fayette Urban Co. Gov.
Department of Law
200 East Main Street
Lexington, KY 40507

Hon. David F. Boehm
Boehm, Kurtz & Lowry
36 East Seventh Street, Suite 2110
Cincinnati, Ohio 45202

Hon. John N. Hughes
124 West Todd St.
Frankfort, KY 40601

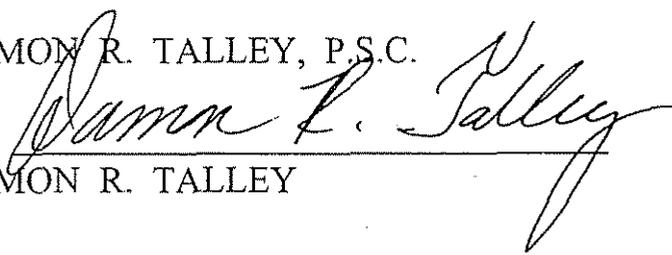
Hon. Thomas J. FitzGerald
Kentucky Resources Council, Inc.
PO Box 1070
Frankfort, KY 40602

Hon. Stephen Reeder
Kentucky River Authority
70 Wilkinson Blvd.
Frankfort, KY 40601

Hon. John E. Selent
Dinsmore & Shohl LLP
1400 PNC Plaza
500 West Jefferson Street
Louisville, KY 40202

Hon. Barbara K. Dickens
Louisville Water Company
550 South Third Street
Louisville, KY 40202

DAMON R. TALLEY, P.S.C.

BY: 
DAMON R. TALLEY