

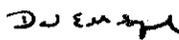
COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF KENTUCKY-AMERICAN)
WATER COMPANY FOR A CERTIFICATE OF) Case No. 2012-00096
PUBLIC CONVENIENCE AND NECESSITY)
AUTHORIZING CONSTRUCTION OF THE)
NORTHERN DIVISION CONNECTION)

Brief of the Attorney General

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I. INTRODUCTION

The legal standard for obtaining a Certificate includes demonstrating a need for such facilities and an absence of wasteful duplication.¹ With regard to “need”:

a showing of a substantial inadequacy of existing service, involving a consumer market sufficiently large to make it economically feasible for the new system or facility to be constructed and operated.

...[T]he inadequacy must be due either to a substantial deficiency of service facilities, beyond what could be supplied by normal improvements in the ordinary course of business; or to indifference, poor management or disregard of the rights of consumers, persisting over such a period of time as to establish an inability or unwillingness to render adequate service.²

Although the Attorney General has a concern that assumptions regarding economic feasibility and the burden on Kentucky American Water (KAW) rate-payers may warrant re-examination as the KAW's rates continue to increase, at present, it appears reasonable to conclude that sufficient demand exists for the facilities under this proposal to be economically feasible. With regard to the inadequacy of the existing facilities, the record does contain evidence of indifference, poor management, and the disregard of the rights of consumers persisting over an extraordinarily long period of time. Accordingly, the Attorney General notes that the evidence supports the issuance

¹ *In the Matter of: The Application of Kentucky-American Water Company For a Certificate of Public Convenience and Necessity Authorizing the Construction of Kentucky River Station II, Associated Facilities and Transmission Main*, Case No. 2007-00134, pages 28 – 30.

² *Id.*; (quoting *Kentucky Utilities Co. v. Public Service Commission*, 252 S.W.2d 885, 890 (Ky. 1952)).

of a Certificate for the facilities sought. KAW's next application for a rate adjustment is the proper forum for addressing issues pertaining to prudence.

II. THERE HAS BEEN AN UNDUE RISK OF FAILURE DURING KAW'S OWNERSHIP OF THE OWENTON WATER TREATMENT PLANT.

Kentucky American Water traces its provision of drinking water service back to 1885 and the creation of the Lexington Hydraulic and Manufacturing Company. Until relatively recently, KAW's drinking water operations were principally in Fayette County with service extending into areas adjacent to Fayette County. This portion of the drinking water service territory is now described as the Central Division, and it has three (3) water treatment plants supplying this area: Kentucky River I; Kentucky River II (KRS II); and the Richmond Road plant.

Kentucky American Water now has a Northern Division. With regard to drinking water, the Northern Division consists of a service territory consequent to KAW's acquisitions of the assets of the Tri-Village Water District, the Elk Lake Property Owner's Association, and certain assets of the City of Owenton. The Northern Division is presently served by a water treatment plant formerly owned by the City of Owenton and through contracts with three (3) other water suppliers. Presently, there is not interconnection between the Central and Northern Divisions. Through this Application, KAW seeks to interconnect its Northern Division to KRS II and re-allocate water from the Central Division to its Northern Division.

The evidence in the record demonstrates that KAW's water treatment plant serving its Northern Division (the Owenton Water Treatment Plant – OWTP) presents an undue risk of failure of service for those who rely upon it for drinking water.³ This has been the situation throughout KAW's ownership of the facilities; therefore, there has throughout KAW's ownership of the facilities been a need for a solution.

Kentucky American Water's relationship with the Owenton Water Treatment Plant began no later than 2001 when KAW began working with the City of Owenton consequent to KAW's purchase of assets of the Tri-Village Water District.⁴ Prior to pursuing of certain assets of the City of Owenton's water and wastewater-related facilities, KAW was aware of various problems with the OWTP including issues associated with its intake facility on Severn Creek.

Evidence from KAW includes:

1. A KAW witness does not know how the OWTP was approved.⁵
2. KAW indicates that it has been extremely fortunate that there has not been an emergency.⁶

³ Excluded from this risk are the customers who rely upon KAW through purchased water from the Carroll County Water District # 1 and the Bullock Pen Water District.

⁴ TE 16 October 2012 (L. Bridwell) 14:50:20 – 14:51:25; see also *In the Matter of: The Verified Joint Application of Tri-Village Water District and Kentucky-American Water Company for the Approval of the Transfer of the Ownership of Assets of Tri-Village Water District to Kentucky-American Water Company*, Case No. 2001-094, Order 8 June 2001, page 4 (Tri-Village purchased water from the City of Owenton).

⁵ TE 16 October 2012 (L. Williams) 11:52:55 – 11:53:18.

⁶ TE 16 October 2012 (K. Cartier) 14:13:50 (very fortunate there has not been a problem).

3. The problem regarding a lack of treatment trains (redundancy) was in existence at the time of the transfer in 2005.⁷
4. There was an issue with the water intake for the Owenton WTP at the time of KAW's purchase.⁸

Thus, the undue risk has been in existence since the first day of KAW's ownership of the facilities serving its Northern Division. KAW's failure to properly address the risk is manifest throughout the record and more than adequately summarized by an 18 November 2008 electronic mail message from KAW's then-Manager of Production Operations regarding the Owenton water treatment plant.

Lance, do you know the status of the investigation about the long term plans for the Owenton Water treatment plant. I know that some were looking into evaluating the site to see the probability of connecting the Owenton distribution network into the new pipeline or should we leave that plant in service. Also, do we know the status of the chemical repair and upgrade project that was planned?

I am hearing rumors that we may want to leave that plant open and not consider connecting it into the New pipeline network and that the plans are to proceed with the chemical upgrades. If this is the case then there is much more work that we need to start planning for. One being a plan for disposing of the residuals which have accumulated at the old plant site. If we are going to continue to operate the existing plant then we need a residuals plan, then we need to get into a budget plan for this.

If you can provide an update on the status or current thinking about the existing plan then we will know more about plans for

⁷ TE 16 October 2012 (K. Cartier) 13:54:30 – 13:54:50; KAW Response to OAG 1 – 9, page 16 of 27; see also KAW Response to OAG 1 – 9, page 3 of 27 (8 October 2004 letter from DOW to Owenton Water Works).

⁸ TE 16 October 2012 (L. Bridwell) 14:51:54 – 14:52:20; see also KAW Response to OAG 2 – 5.

maintenance, equipment, and some more firm multi year operating plans. with residuals disposals and the existing old plant being large items that we need to get an operating plan in place for.⁹

Given the evidence, there is adequate demonstration of a substantial deficiency of service facilities. There is a need for KAW to finally solve this problem.

III. KAW'S EXAMINATION OF ALTERNATIVES WAS IMPROPERLY LIMITED; NONETHELESS, KAW SHOULD BE HELD TO ACCOUNT FOR THE FACT THAT IF IT FELT THAT THE KRS II INTERCONNECTION WAS THE ONLY OTHER OPTION, IT SHOULD HAVE MADE THIS KNOWN DURING THE PLANNING OF THE KRS II FACILITY.

Kentucky American Water has a responsibility to conduct an examination into reasonable alternatives. In this instance, KAW, without actually contacting any of the neighboring utilities, made the decision that the only options were through substantial investment in the OWTP or substantial investment through an interconnection with the KRS II facility. KAW's diligence with respect and corresponding documentation of the identification of alternatives is not adequate.

At this stage, though, with KAW's customers at a continuing risk for a failure of the OWTP, it is not clear that further research into additional alternatives would produce material benefit sufficient to outweigh the costs associated with a failure of the OWTP. Nonetheless, because KAW identifies substantial work on the OWTP and an interconnection with the KRS II facility as the only reasonable alternatives, then KAW

⁹ KAW Response to PSC 1 – 3, page 47 of 147; see also KAW Response to OAG 2 – 36.

should be held to account for the fact that it did not adequately incorporate this fact into its planning for the KRS II facility. Simply enough, KAW knew that the OWTP design was flawed from "get go,"¹⁰ and it appears to have made a conscious decision to ignore an interconnection with the KRS II facility during the planning and pursuit of approval of that facility.

The KRS II facility was built to address the water supply and water treatment needs of KAW's Central Division. While KAW is confident that KRS II has capacity well-above the 20 MGD necessary to address the risks of the Central Division,¹¹ the Attorney General is quite concerned about the re-allocation of this capacity. Again, the KRS II design, as stated by KAW, was for its Central Division. With re-allocation, a precedent will be set for further re-allocations of capacity away from the Central Division. KAW's position that problems consequent to re-allocation can be solved by simply accelerating the expansion of the KRS II facility¹² provides no comfort.

IV. CONCLUSIONS AND RECOMMENDATIONS

The legislature assigns the Kentucky Public Service Commission the responsibility to review applications of jurisdictional utilities that seek to undertake major construction projects. The Commission reviews the applications and determines

¹⁰ TE 16 October 2012 (L. Williams) 11:52:55 – 11:53:18.

¹¹ And, that the KRS II capacity is actually 20% above the amount that was proposed as necessary raises a moderate concern in that the variance between the proposed versus actual is quite significant.

¹² KAW Response to OAG 1 – 29(B); KAW Response to OAG 2 – 42(C).

matters within the scope of its authority. In this instance, the evidence supports the issuance of a Certificate. This position should not be interpreted as a concession by the Attorney General that KAW's investigation of alternatives was sufficient and reasonable and that KAW's actions with regard to the OWTP have been prudent.

It is also important to point out that the KRS II facility was a remarkably controversial project, and reasonable steps to reduce controversies and promote better planning are in the public interest. KAW, itself, chose to point to the encouragement for it to become a regional supplier of water as well as three other factors (compliance with safe drinking water legislation and other regulatory compliance, economies of scale, and inadequacies of sources of supply) in seeking approval of the transfer of ownership and control of certain assets owned by the City of Owenton.¹³ Yet, in terms of leadership, KAW, which has a member of its senior management serving on the Kentucky River Authority's Board, did not even bother to provide an informal presentation of its plan to the Kentucky River Authority.¹⁴ That is not leadership.

If this Commission continues to encourage KAW to be a regional supplier of water, then the Attorney General respectfully requests that the Commission provide equal encouragement for KAW to show leadership in water supply and water resource

¹³ Case No. 0005-00206, Verified Joint Application for Approval of the Transfer of the Ownership of Certain Water and Wastewater-Related Assets of the City of Owenton, pages 2 and 3; see also KAW Response to OAG 2 – 31, attachment 1, page 1 of 43 (OWTP had history of water supply limitations during dry weather conditions).

¹⁴ KAW Response to OAG 1 – 13.

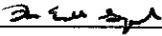
planning for the Kentucky River Basin. The Kentucky River Authority has a statutory assignment to develop comprehensive plans for the management of the Kentucky River within the basin, including a long-range water resource plan and a drought response plan.¹⁵ KAW's neglect in terms of sharing information - **even informally** - with the KRA is consistent with a "siloed" approach to water resource planning, and such an approach unnecessarily places us (the Commission, KAW, LFUCG, the OAG, and others) squarely on the path to experience a repeat of the controversy and acrimony of the approximate quarter-century battle over how best to meet the water supply needs of KAW's Central Division.

¹⁵ KRS 151.720(11).

Notice of Filing, Certificate of Electronic Filing, and Certificate of Service

Pursuant to Ordering Paragraphs 3, 13, and 14 of the Commission's 20 March 2012 Order of procedure, the Attorney General will submit the original and one photocopy in paper medium on 16 October 2012, and he has submitted one copy in electronic format by uploading the electronic file to the Commission's Web Application Portal on this 15th day of October 2012.

Pursuant to Ordering Paragraphs 10 and 11 of the Commission's 20 March 2012 Order of procedure, counsel certifies that the electronic filing is a true and accurate copy of the document filed in paper medium. Further, the electronic version of the filing has been transmitted to the Commission, and the Attorney General has transmitted notice to the other parties of record. There are no parties that have been excused from participation by electronic means. The date for this action is 15 November 2012.


Assistant Attorney General