

Case No.: 2005-00174
Questions From: Public Service Commission – October 7, 2005
Response from: Hopkinsville Water Environment Authority
Sponsoring Witness: Lennis Franklin Hale

INFORMATION REQUEST NO. 7.

The filing requirements for forecasted or budgeted financial information to support an increase in rates are set forth in KRS 278.192 and 807 KAR 5:001, Section 8. Explain why the Commission should not require HWEA to comply with these requirements for any proposed rate adjustment that is based upon future or projected operations.

RESPONSE:

HWEA objects to Commission Second Information Request No. 7 to the extent it seeks a legal conclusion. However, without waiving its objection to Commission Second Information Request No. 7, HWEA provides the following Response.

Municipal utilities are not subject to the jurisdiction of the Commission except in their relationship with Commission-regulated utilities. *See Simpson County Water Dist. v. Franklin, Ky., 872 S.W.2d 460, 462 (1994).* HWEA does not understand that the provisions of KRS 278.192 apply to it as it is not a “utility” as defined therein.

The provisions of KRS 278.192 are permissive (“shall allow”) and not mandatory (as they do not state “shall require”).

The rates proposed by HWEA are supported by the B&V Report which is based on sound ratemaking methodology as outlined in the B&V Report and the Prefiled Testimony of Jennings Rowe McKinley II.

The wholesale rate methodology used in the B&V Report was approved by the Commission in its December 17, 2003 Order in Case No. 2003-00087 styled *In the matter of: Investigation of the Hopkinsville Water Environment Authority Wholesale Rate to Christian*

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County Water District. HWEA’s interpretation of the Commissioner’s Orders in Case No. 2003-00087 seems to be consistent with the recent decision in *City of Greenup v. Public Service Commission*, 2005 WL 1540169 (Ky. App. 2005) (*Motion For Discretionary Review Pending*).

The Commission did not require HWEA to comply with KRS 278.192 in either Case No. 2003-00087 or at any prior time in this proceeding.

The Commission did not require the Christian County Water District (“CCWD”) to comply with the similar requirement in its Application in Case No. 2005-00391 styled *In the matter of: Application Of Christian County Water District To Issue Securities In The Approximate Principal Amount Of \$3,305,000 For The Purpose Of Refunding Certain Outstanding Revenue Bonds Of The District Pursuant To The Provisions Of KRS 278.200*.

Therefore, to the extent necessary, HWEA requests a deviation from the requirements described in Commission Second Information Request No. 7, pursuant to 807 KAR 5:001 Section 14, because HWEA has demonstrated good cause to deviate from those requirements for all of the reasons set forth above.

Finally, the rates proposed by HWEA, based on the B&V Report, produce fair and equitable rates related to the costs expended by HWEA to provide service to the CCWD. *See* KRS 278.030 and OAG 78-656.

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INFORMATION REQUEST NO. 8.

Refer to table 14 of the Cost-of-Service Study at line 15, Payments to the Christian County Water District (“Christian Water”). The stated purpose of payments to Christian Water is for reimbursements for overpayments as explained on page 12 of the Cost-of-Service Study. Explain why a portion of this payment is allocated to the wholesale customer, Christian Water.

RESPONSE:

The overpayment by the CCWD was applied to operating expenses applicable to all customer classes including the CCWD, therefore, the reimbursement for overpayment is similarly allocated to all customer classes including the CCWD.

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INFORMATION REQUEST NO. 9.

Refer to HWEA’s Responses to Staff’s First Request, Item 19, the Direct Testimony of J. Rowe McKinley in the Public Hearing on Proposed Water and Wastewater Rates 2001, Water Department of Philadelphia, Pennsylvania at 65. Explain how the proposed rate schedule is consistent with Mr. McKinley’s position that “Practicability also requires that rates be reasonably simply in application and subject to as few misinterpretations as possible.”

RESPONSE:

The proposed rate schedule is straight forward and consistent with the existing schedule of rates and is a commonly used block rate form. We see no inconsistency between the statement referenced in the question and the proposed rate schedule.

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INFORMATION REQUEST NO. 10.

Provide all HWEA budget instructions, assumptions, directives, manuals, policies and procedures, timelines, and descriptions of budget procedures.

RESPONSE:

Although HWEA is unsure of the information that is sought by Commission Second Information Request No. 10, it will do its best to provide an appropriate Response. Beginning in March of a given year, the General Manager of HWEA notifies each Department Director that the draft budgets for each Department are due by the third Friday in April. A copy of last year's budget, YTD financial statements and projected cost of living raise is provided to each Department Director at that time. The General Manager works on revenue projections during this period. Each Department Director meets with the supervisors and develops a draft budget for the following departments: Water Administration, Source of Supply, Moss WTP, Water Distribution, Water Technical Services (Engineering), Human Resources and Health and Safety. Two budgets are prepared by each department: operating and capital. The capital budget complies with the Five Year Plan for HWEA. A description of the operating budget process was supplied in HWEA's Response to Commission Information Request Nos. 3.b. and 3.c.

After review by the General Manager, the draft budgets are compiled and presented to the HWEA Board of Commissioners at the May Meeting. The Board considers the draft budget for a month and can request additional information or ask questions prior to voting on the proposed operating budget at the June Meeting. At the June meeting, the Board approves the operating budget for the following fiscal year.

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After the Board has adopted the operating budget, “Budget Monitoring Reports” are prepared monthly for the Department Directors and Supervisors. The Directors and Supervisors use the monitoring reports to gauge their compliance with the budget. Adjustments may be made during the course of the fiscal year to accommodate unusual circumstances that affect the operating budget, such as increased chemical costs in response to degradation in the quality of the raw water or an unforeseen increase in energy costs. Over the past five years, actual expenditures ranged from less than 5% over budget to 3% under budget. This range is well within general accounting principles for budgeted versus actual expenditures.

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INFORMATION REQUEST NO. 11.

Describe the process that HWEA uses to plan and approve construction projects.

RESPONSE:

Generally HWEA does not implement a construction project that is not contained in the Five Year Plan adopted by the HWEA Board of Commissioners. The process of preparing and maintaining the Five Year Plan was presented by HWEA's Response to CCWD Data Request No. 20.

Each year in December, the General Manager of HWEA distributes the current edition of the HWEA Five Year Plan to the Department Directors and Supervisors for review and consideration in developing the subsequent year's edition of the Five Year Plan. From operating experience the Directors or Supervisors may move up a project from some future year or nominate a new project. Lastly the General Manager and Director of Technical Services agree on a draft Five Year Plan to be presented to the HWEA Board of Commissioners in February.

Many of the projects contained in the Five Year Plan are designed in-house by HWEA's engineering department. Typically these projects are also constructed by HWEA's Distribution Department crews. These projects are also generally funded from HWEA's reserve funds. Larger projects are designed by engineering consultants, bid to independent contractors and are funded by outside sources such as bonds or low interest loans.

HWEA begins planning for upgrades to treatment plants, once the average daily treatment level meets 80% of the capacity of the plant. HWEA also is involved in an annual program of replacing all small diameter, galvanized water mains in the system. HWEA also

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replaces a certain number of Bourbon fire hydrants annually. Deteriorating water capacity, quality and pressure is also considered in replacing or upgrading water mains. HWEA, by maintaining an experienced and qualified staff, can best respond to needed improvements and upgrades of the system, while keeping user charges low. According to a recent State Water Rate Survey, HWEA has the second lowest water rates in the Pennyrite ADD and the 4th lowest rates in Western Kentucky.

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INFORMATION REQUEST NO. 12.

a. For each construction project that HWEA has commenced since January 1, 2000 through December 31, 2004, provide the following in the format set forth in Schedule 1:

- (1) Project number.
- (2) Project title and description.
- (3) Annual actual cost.
- (4) Annual original budgeted cost.
- (5) Variance between annual actual cost and annual original budgeted cost in dollars.
- (6) Variance between annual actual cost and annual original budgeted cost as a percentage.
- (7) Percentage of total construction budget that proposed project comprises for the budgeted year.
- (8) Total actual project cost.
- (9) Total budgeted project cost.
- (10) Variance between total actual project cost and total budgeted project cost.
- (11) Date the original budget projected the project to start.
- (12) Date the original budget projected the project to be completed.
- (13) Date construction of project actually commenced.
- (14) Date construction of the project was actually completed.

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RESPONSE:

A spreadsheet labeled Attachment 12-1 containing the relevant information requested is attached hereto as Exhibit 12.a. Not all information requested by the Commission is available. Only one water project began by HWEA during the reporting period was a multi-year project: Phase One of the Lake Barkley Raw Water Project. Therefore the spreadsheet has combined into one column the following: Annual actual cost and total project cost, annual original budgeted cost and total budgeted project costs, variance between annual actual cost and annual original budgeted cost and variance between total actual project cost and total budgeted project costs, and the variances expressed as percentages. The annual and total project costs are the same for the one-year projects. A separate spreadsheet labeled Attachment 12-2 has been provided for the Phase One Lake Barkley Raw Water Project and is also attached hereto as part of Exhibit 12.a. Only the dates for the start of construction and the completion of construction are provided.

HWEA installs the water mains for private developments both off-site and on-site. In addition HWEA crews install many water mains which are fully reimbursed by the owner. These fully reimbursed projects are also reported on the spreadsheet referred to above.

Unless the construction project was funded by indebtedness there was no impact of the project on the wholesale rate charged to the CCWD. Black and Veatch considered the increase in HWEA's water assets in the Cost of Service Study, however construction cost expended during the year from HWEA's reserves do not appear as expenditures in HWEA's financial statements.

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b. For each project in which a variance between actual and budgeted cost occurred or in which a delay in its start or completion occurred, describe the variance or delay and the reasons for such variance or delay.

RESPONSE:

The variances between the budgeted project cost and the actual project costs for the reported projects were all minor, less than 5%. There are several reasons why the actual costs varied from the budgeted (estimated) costs. In most cases, more or less solid rock excavation occurred than anticipated. Weather also plays a major role in the cost of a project. For projects constructed using force account, supplies used from inventory could be a different price than materials which had to be purchased at the time of construction. However, HWEA does not have a specific explanation for the variances reported for the subject construction projects.

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INFORMATION REQUEST NO. 13.

Provide all correspondence between HWEA and Black & Veatch regarding the preparation or review of the Cost-of-Service Study and the development of the proposed wholesale rate.

RESPONSE:

A copy of all correspondence between HWEA and Black & Veatch regarding the preparation or review of the B&V Report is also on the CD attached hereto as Exhibit No. 1.

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INFORMATION REQUEST NO. 14.

Refer to the HWEA's Response to Christian Water's First Information Request, Item 9(b). Explain why it is reasonable or appropriate for the Commission to establish a wholesale rate to be assessed to Christian Water for service rendered on or after February 13, 2006 that is based in part on the costs related to the Lake Barkley raw water main, which is not likely to be completed and placed into service until late 2006 or 2007.

RESPONSE:

As shown on Line 1 of Table 7 in the B&V Report, construction on the raw water line will begin in FY 2006. Revenue bonds were issued in May 2005 to fund the project and full debt service on the Series 2005A Bonds will be in effect in FY 2006.