

Commonwealth of Kentucky
Before the Public Service Commission

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COMMISSION

In the Matter of:

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

BRIEF OF THE ATTORNEY GENERAL

Respectfully submitted,

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INTRODUCTION

The Kentucky-American Water Company seeks authorization for the construction of a water treatment plant on Pool 3 of the Kentucky River as well as additional facilities including a transmission main. The Commission, pursuant to its authority under KRS 278.020(1), must determine whether the “public convenience and necessity require the service or construction.”

SUMMARY OF THE ATTORNEY GENERAL’S RECOMMENDATION

An applicant seeking authorization of construction through a certificate of convenience and public necessity must demonstrate both need and the absence of wasteful duplication. It is clear that there is a need for a water supply project and a corresponding need for additional treatment capacity. There is, however, an issue regarding the economic feasibility of this proposal.

Moreover, the Kentucky-American Water Company plan does not demonstrate the absence of wasteful duplication. Accordingly, the Attorney General cannot recommend approval of the plan as filed.

The Public Service Commission must condition the approval of the Kentucky-American Water Company plan on the acceptance of a cost cap¹. With a cost cap, the record stands to provide adequate protection on the issue of economic feasibility and adequate evidence of the absence of wasteful duplication.

¹ The Commission should also incorporate into any approval two additional conditions, a conservation program and water supply and demand management plan, previously accepted by KAWC during this proceeding.

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APPLICABLE LEGAL STANDARD FOR REVIEWING THE PROPOSAL

KRS 278.020 requires the issuance of a certificate of convenience and necessity prior to “the construction of any plant, equipment, property, or facility for furnishing to the public any of the services enumerated in KRS 278.020.” The enumeration of services under KRS 278.020 include the “the diverting, developing, pumping, impounding, distributing, or furnishing of water to or for the public, for compensation.”²

Kentucky-American Water Company, as the applicant, has the burden of proof.³ While there are several reported opinions of the Kentucky judiciary that discuss the requirements for obtaining a certificate, two cases in particular and in tandem set forth the legal framework for an application for construction.

In *Kentucky Utilities Company v. Public Service Commission*, 252 S.W.2d 885 (Ky. 1952), the judiciary notes the following two factors for considering issues relating to need.

We think it is obvious that the establishment of convenience and necessity for a new service system or a new service facility requires first a showing of 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.

² KRS 278.010(3)(d). The Kentucky-American Water Company does not contest the necessity of prior authorization for this construction project. Further, KAWC is not a retail electric supplier nor is this project “an ordinary extension of existing systems in the usual course of business.” Thus, the proposal does not fall within the exceptions set forth in KRS 278.020(1).

³ *Energy Regulatory Commission v. Kentucky Power*, 605 S.W.2d 46, 50 (Ky. App. 1980).

Second, the 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.⁴

The above two factors necessarily include consideration of whether there is a current excess of capacity over need.⁵ In *Kentucky Utilities Company v. Public Service Commission*, 390 S.W.2d 168 (Ky. 1965), the judiciary provides further discussion of certificate proceedings. With regard to demonstrating need (the absence of a current excess of capacity over need), “the deficiency is not to be measured by the needs of the particular instant, but by “immediately foreseeable needs.”⁶ “The immediately foreseeable future may embrace a number of years.”⁷ Further, with regard to feasibility, a proposal is feasible if it is “capable of supplying adequate service at reasonable rates.”⁸ The Commission, therefore, must consider the impact on rates.⁹

If the applicant is able to establish that there is a need for a new system or facility (and a consumer market sufficiently large to make the project economically feasible), then the applicant must demonstrate the absence of “wasteful duplication.” For this aspect of the test, the Court notes the following:

⁴ *KU v. PSC*, 252 S.W.2d at 890.

⁵ *KU v. PSC*, 252 S.W.2d at 890 (The definition of “duplication” includes, but is not limited to, the concept of having an excess of capacity over need.)

⁶ *KU v. PSC*, 390 S.W.2d at 171 citing *KU v. PSC*, 252 S.W.2d 885 (Ky. 1952).

⁷ *KU v. PSC*, 390 S.W.2d at 171.

⁸ *KU v. PSC*, 390 S.W.2d at 175.

⁹ See, for comparison, *In the Matter of: The Application of East Kentucky Power Cooperative, Inc. For a Certificate of Public Convenience and Necessity to Construct a 138 KV Transmission Line in Rowan County, Kentucky*, Case No. 2005-00089, Order, 9 November 2005.

We think that “duplication” also embraces the meaning of an excessive investment in relation to productivity or efficiency, and an unnecessary multiplicity of physical properties, such as right of ways, poles and wires.¹⁰

Thus, duplication embraces both economic and physical aspects of the proposal. Additionally, implicit in the second analysis is the inquiry into whether the proposal will result in an excessive amount of capacity over need. Thus, the applicant must demonstrate both the current absence of excess capacity over need as well as the continuing absence of excessive capacity over need after implementation of the project.

There are limits to the Commission’s jurisdiction. The Commission will not select between KAWC’s proposal and the LWC proposal. The Commission will act only on the pending application.¹⁵ Second, the Commission’s powers are purely statutory, and “it cannot decide issues not subject to its jurisdiction.”¹⁶

¹⁰ *KU v. PSC*, 252 S.W.2d at 890. This latter aspect includes “economic loss through interference with normal uses of land, that may result from multiple sets of right of ways, and a cluttering of the land with wires and poles.” *KU v. PSC*, 252 S.W.2d at 892.

¹⁵ Order, 26 November 2007 (“Only one proposal is before the Commission. LWC has not made an application to this Commission for the construction of facilities nor does it have a direct and immediate interest in Kentucky-American’s proposal.”)

¹⁶ See, for example, *In the Matter of: The Application of East Kentucky Power Cooperative, Inc. For a Certificate of Public Convenience and Necessity to Construct a 161 KV Transmission Line in Barren, Warren, Butler, and Ohio Counties*, Case No. 2005-00207, Order, 31 October 2005 (Federal laws such as the National Historic Preservation Act and the National Environmental Policy Act are not within the Commission’s jurisdiction.)

ARGUMENT

1. Need

- A. There is a substantial inadequacy in Kentucky-American Water Company's existing sources of supply and treatment capacity.

The first test that Kentucky-American must pass is establishing that there is a need for a project.¹⁷ "Need" as contemplated under the case law, includes consideration of economic feasibility. For this project, there is a water supply inadequacy and a separate treatment capacity inadequacy.¹⁸

With regard to water supply, the Commission has already made findings on this point. Specifically, in Case No. 93-434 the Commission found, for the planning horizon through the year 2020, "a water supply deficit would exist during an extreme drought situation."¹⁹ Moreover, the Commission also found "that the net effect of the Kentucky River Authority's activities, if implemented will be insufficient" in terms of the development of an adequate and reliable source of water supply for Pool 9.²⁰ Thus, Pool 9 is inadequate to meet Kentucky-American Water Company's drought requirements through the year 2020.

"All of the evidence in this case [No. 93-434] supports the conclusion that the Kentucky River [at Pool 9] cannot supply enough water to meet the unrestricted demands of Kentucky-American's customers during drought

¹⁷ *Kentucky Utilities Co. v. Public Service Commission*, 252 S.W.2d 885, 890 (Ky. 1952).

¹⁸ TE Vol. I of III, page 130; (While LWC may contest the magnitude of the inadequacies, LWC concedes the existence of treatment and source inadequacies. VR 3/05/08; 9:52:43 to 9:53:07).

¹⁹ Case No. 93-434, Order, 21 August 1997, page 5.

²⁰ Case No. 93-434, Order, 21 August 1997, page 5. The Attorney General challenged this finding; however, the Kentucky River Authority, which was a party to the proceeding, did not.

conditions.”²¹ Hence, the Commission, in a prior investigation, has already made the determination that there is a water supply inadequacy.

While it is wise to reconsider the prior findings of Case No. 93-434, the record in this proceeding does not compel a change in those findings. First, the Kentucky River Authority was a party to Case No. 93-434, and it did not challenge the findings in that proceeding. The KRA is a party to this case, and it has not asked the Commission to revise those findings based upon new information or subsequent developments.

Second, although there appears a consensus that the Kentucky River Authority will take further action to augment the water supply in Pool 9 via a crest-gate or other facility, at present, this augmentation has not taken place. Further, the amount of additional augmentation via a project on Dam 10 or other dams upstream of Pool 9 is unknown and uncertain. Pool 9, for at least the near term, does not and will not provide a sufficient supply of water.²²

The Attorney General has consistently fought against any notion that Kentucky-American Water Company can use the goal of supplying the unrestricted demand of its customers during a drought of record as a planning objective. The Attorney General continues to assert that conservation and demand management are necessary (and under-utilized). Nevertheless, with regard to need and the supply at Pool 9, this is not simply a lawn-watering issue.

²¹ Case No. 93-434, Order, 21 August 1997, pages 2 and 3.

²² TE Vol. II of III, pages 229 and 230 (Rubin: In severe drought, KAWC cannot even come close to meeting reasonable demand.); (CAWS, through its witness, indicates that it has no idea as to whether the KRA will place crest gates on Dams 9 or 10, and that it cannot predict the KRA. VR 3/05/08; 4:55:45 to 4:56:34).

As noted in the December 1996 Executive Summary of the Kentucky River Basin Water Supply Assessment Study prepared for the Kentucky River Authority²³ by The Kentucky Water Resources Research Institute (and which is part of the record in this case by virtue of its incorporation):

If all withdrawals from the Kentucky River are held at their winter levels, the 3.0 billion gallon residual deficit in Pool 9 (i.e. 2020 high demand conditions) can be reduced to 1.1 billion gallons. It should be recognized that this represents an extreme demand management policy and one that would likely result in millions of dollars of damages as well as adverse ecological impacts. Since such a strategy does not completely eliminate the remaining deficit, it is recommended that demand management not be used as a primary means of eliminating the remaining 3.0 billion gallons, but that it be used to supplement one of the remaining water-supply alternatives.²⁴

It is not reasonable to proceed under the assumption that conservation can eliminate the need for a new supply project.²⁵ Likewise, more aggressive control by Kentucky-American Water Company of its non-revenue water will not eliminate the need for a new water supply project.²⁶ While conservation and control of non-revenue water are critical, optimization in these areas will not eliminate the need for access to additional water supply.

With regard to treatment capacity, there is also a substantial inadequacy. As noted, a "deficiency is not to be measured by the needs of the particular

²³ The Kentucky River Authority has the responsibility for water supply planning and drought response planning for the Kentucky River Basin. KRS 151.720.

²⁴ Executive Summary, Kentucky River Basin Water Supply Assessment Study (Kentucky Water Resources Research Institute, December 1996).

²⁵ OAG, Pre-filed Direct Testimony, Rubin, page 10; TE Vol. II of III, pages 184, 236, and 279.

²⁶ OAG, Pre-filed Direct Testimony, Rubin, pages 11 through 13; TE Vol. II of III, pages 236 and 279.

instant, but by ‘immediately foreseeable needs,’²⁷ and “the immediately foreseeable future may embrace a number of years.”²⁸

Kentucky-American Water Company is using the period running through the year 2030 as its planning horizon. The 2030 planning horizon is reasonable. It is the essentially the same term of years for a planning horizon found reasonable by this Commission in Case No. 93-434. Given that KAWC is able to support its demand projections through the end of this period through population projections by the Kentucky State Data Center,²⁹ the end of the period is not too remote to render the demand projections the product of unreasonable speculation. Moreover, given the fact that, regrettably, it has been approximately two decades from the identification of a problem to the filing of a certificate to address the problem, anticipating the needs of Kentucky-American Water Company through the year 2030 is not too remote.³⁰

KAWC’s demand projections over this period estimate a growth in Average Day Demand from 45.91 mgd (2006 actual results) to 47.08 mgd in year 2030.³¹ By comparison, KAWC estimates a growth in Total Maximum Day Demand from 67.22 mgd (2006 actual results) to 81.67 mgd in year 2030.³² Thus, Kentucky-American Water Company, with a total “base” treatment capacity of

²⁷ *KU v. PSC*, 390 S.W.2d at 171 citing *KU v. PSC*, 252 S.W.2d 885 (Ky. 1952).

²⁸ *KU v. PSC*, 390 S.W.2d at 171.

²⁹ TE Vol. II of III, pages 9 and 10.

³⁰ See, for comparison, *Kentucky Utilities Co. v. Public Service Commission*, 390 S.W.2d 168, 172 (Ky. 1965).

³¹ Application, Direct Testimony of Linda Bridwell, Table 1.

³² Application, Direct Testimony of Linda Bridwell, Table 1.

65 mgd and a current treatment capacity rating of 70 mgd,³³ projects year 2010 treatment capacity deficits of 5.87 mgd to .87 mgd for its Total Maximum Day Demand.³⁴ Under a "Hot, Dry Scenario," the deficit numbers for year 2010 are 10.33 mgd and 5.33 mgd respectively.³⁵

For the end of the planning horizon, Kentucky-American Water projects year 2030 treatment capacity deficits of 16.65 mgd and 11.65 mgd for its Total Maximum Day Demand.³⁶ For a "Hot, Dry Scenario," the deficit numbers for year 2030 are 21.6 mgd and 16.6 mgd respectively.³⁷

While there may still be room for further refinement in the model through which Kentucky American Water Company projects demand, overall, the model, which has been the subject of much scrutiny, produces sufficiently reliable results for estimating demands.³⁸ Considering the estimates of demands over the planning horizon, which now extends to the year 2030, there is a substantial treatment capacity deficit.³⁹

³³ The Kentucky Division of Water has granted Kentucky-American Water Company a temporary re-rating of its Kentucky River Station to 45 mgd during summer months. Application, Direct Testimony of Linda Bridwell, page 30.

³⁴ Application, Direct Testimony of Linda Bridwell, Table 1.

³⁵ Application, Direct Testimony of Linda Bridwell, Table 2.

³⁶ Application, Direct Testimony of Linda Bridwell, Table 1.

³⁷ Application, Direct Testimony of Linda Bridwell, Tables 1 and 2.

³⁸ With regard to demand projections, LWC does not appear to call into question KAWC's model for projecting demand. Rather, LWC criticism appears directed at the gap between KAWC's demand in the near term and KAWC's statements regarding the "Day 1" need to reserve capacity and take a minimum flow of 10 or 12.5 mgd. CAWS certainly calls into question KAWC's demand projections; however, the model through which CAWS projects demand is, at best, novel. There is not a sufficient basis for utilizing the CAWS model (or asserting that the CAWS results are more reliable).

³⁹ TE Vol. II of III, pages 229 and 230.

- B. It is unclear whether KAWC's consumer market is sufficiently large to make it economically feasible for the new facilities to be constructed and operated.

The Commission has given Kentucky-American Water Company a specific instruction with regard to KAWC's responsibility for an adequate and reliable source of water supply.

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 requirements of its customers under maximum consumption through the year 2020.⁴⁰

While it may be argued that implicit in this mandate is the finding that Kentucky-American Water Company's market is sufficiently large to allow an economically feasible project, the issue of economic feasibility **was not** within the scope of questions determined in Case No. 93-434.⁴¹ Further, such an argument rests upon the theory that the cost of the project is not relevant. The Order in Case No. 93-434 does not suggest such a result.

In *Kentucky Utilities Company v. Public Service Commission*, 390 S.W.2d 168, 172 (Ky. 1965), the Court notes:

As we view it, the question of whether the consumer market in the immediately foreseeable future will be sufficiently large to make it economically feasible for a proposed system or facility to be constructed ... is not one which must be answered with absolute certainty; it is sufficient that there is a reasonable basis of anticipation.

⁴⁰ *In the Matter of: An Investigation of the Sources of Supply and Future Demand of Kentucky-American Water Company*, Case No. 93-434, Order, 21 August 1997, page 6.

⁴¹ Case No. 93-434, Order, 21 August 1997, page 2 ("The only issues before us now are the adequacy of Kentucky-American's sources of supply and the magnitude of any deficiency.")

The Office of the Attorney General does not believe that evidence concerning the projections of the number of customers, standing alone, is sufficient evidence of a consumer market providing economic feasibility. Economic feasibility necessarily entails whether the economic burden on the consumers in the market will be excessive.⁴² The requirement is a fundamental consumer safeguard that is a condition precedent to an issuance of a certificate.

While the record in this case is extensive, it is difficult to identify any portion of the record that answers the issue of economic feasibility. With a “typical” residential customer who uses 700 cubic feet per month as a proxy, the corresponding bill for such usage is \$24.31.⁴³ “The Kentucky River solution to the KAWC source of supply deficit would raise the current average residential bill of KAWC by approximately \$8.62 per month.”⁴⁴

The purpose of the requirement on this point is for the applicant to consider the impact of the project on the individuals who will be called upon to pay for the project and to **prevent** an economically infeasible project or an

⁴² Consider *Kentucky Utilities Company v. Public Service Commission*, 390 S.W.2d 168, 172, 173 (Ky. 1965)(feasibility includes an assessment of whether the rates will be reasonable).

⁴³ See, for current rates, *In the Matter of: Adjustment of Rates of Kentucky-American Water Company*, Case No. 2007-00143, Order, 29 November 2007, Appendix A, page 1. The calculation: $(7 \times 2.33779) + \$7.95 = \24.31 .

⁴⁴ VR 3/06/08; 10:40:20 to 10:40:51; KAWC response to Citizens for Alternative Water Solution’s Second Supplemental Data Requests, Item 4; TE Vol. III of III, pages 120, 121; compare with KAWC Responses to PSC Post-Hearing Data Request, Item 9 - \$8.75 increase in average residential monthly bill.

excessive rate. An increase of approximately 37% for the typical residential customer (attributable to this proposal alone) is quite significant.⁴⁵

The Commission is free to take administrative notice of the rates of other jurisdictional utilities as well as trends in those rates. Those rates, however, are set in rate proceedings. In this Application the analysis of the potential rates result from a projection. In the absence of cost cap, it is far too speculative to compare the projected rates to existing rates of other utilities and draw the conclusion that the project is economically feasible. Moreover, economic feasibility focuses upon a specific customer market rather than general industries standards.⁴⁶ Finally, argument that Kentucky-American's project is lower in total cost than the LWC project does not address this point. It may be the case that neither project is economically feasible.

Rather than trying to prove a negative (that the record does not contain adequate evidence of economic feasibility), the Attorney General notes that demonstrating economic feasibility is a burden falling upon Kentucky-American Water Company. In the absence of a cost cap, the record regarding economic feasibility does not provide a sufficient basis for approval of this project. Because, ultimately, KAWC customers bear the risk of any evidentiary failure on this point, the use of a cost cap is essential for protecting the public interest.

⁴⁵ Additionally, there would also be increases to other customers as well. The OAG uses the "typical" residential customer for explication because the residential class is the largest customer group in terms of number of customers and the residential rate classification generates, among the rate classifications, the largest amount of operating revenues.

⁴⁶ A rate that is economically feasible for one market may not be economically feasible in a different location (for a different group of customers).

- C. The inadequacy in Kentucky-American Water Company's sources of supply is due to a substantial deficiency beyond what could be supplied by normal improvements in the ordinary course of business.

Kentucky-American Water Company's source of supply deficiency at Pool 9 is a substantial deficiency.⁴⁷ The Commission has already made the determination in Case No. 93-434.⁴⁸

- D. The inadequacy in its treatment capacity is due to a substantial deficiency of service facilities beyond what could be supplied by normal improvements in the ordinary course of business.

Kentucky-American Water Company's treatment capacity deficiency is a substantial deficiency. Over the planning horizon, which extends to 2030, the treatment capacity deficit could not be supplied by normal improvements in the ordinary course of business.⁴⁹

2. Wasteful Duplication

- A. The project does not appear to result in an excess of capacity over need.

The second test that Kentucky-American must pass is establishing the **absence** of wasteful duplication.⁵⁰ The second test requires two basic considerations. A simple way to describe the test is to convey that the second test focuses upon the ability of the plan to meet an identified need at the lowest

⁴⁷ The Attorney General incorporates by reference his prior water supply deficit argument in Section 1 A.

⁴⁸ See, generally, Case No. 93-434, Order, 21 August 1997.

⁴⁹ The Attorney General incorporates by reference his prior treatment capacity deficit argument in Section 1 A.

⁵⁰ *Kentucky Utilities Co. v. Public Service Commission*, 252 S.W.2d 885, 890 (Ky. 1952).

reasonable cost while minimizing physical properties. A brief description of the project is necessary.

Kentucky-American Water Company's proposal is "the construction of a raw water intake, raw water pumping station, and water treatment station located adjacent to Pool 3 on the Kentucky River with an associated transmission main and required booster station and water storage tank."⁵¹ The design of the pumping and treatment facilities calls for an initial treatment capacity of 20 mgd (expandable to 30 mgd⁵²) and a hydraulic capacity of 30 mgd.⁵³

"The intake, pumping station and water treatment plant will be located approximately two miles north of Swallowfield on the Kentucky River along the Owen and Franklin County line."⁵⁴ In order to move the water from this site to KAWC's central Kentucky service territory, the project includes a plan to install approximately 160,000 linear feet of a 42-inch transmission main.⁵⁵

As described previously in Section 1 A, Kentucky-American Water Company is using a planning horizon that ends in the Year 2030. The projection is that Kentucky-American Water Company will need additional treatment capacity for meeting its Maximum Day Demand (for a Hot, Dry Scenario) in the amounts of approximately 16.79 mgd by the year 2020 and 21.6 mgd by the year 2030.⁵⁶ The need for additional treatment capacity amounts for meeting its

⁵¹ Application, page 5, Numbered Paragraph 11.

⁵² Application, Exhibit A – Specifications Volume III, page 1.

⁵³ Application, Exhibit A – Specifications Volume III, page 1.

⁵⁴ Application, pages 5, 6, Numbered Paragraph 12.

⁵⁵ Application, pages 5, 6, Numbered Paragraph 12.

⁵⁶ Application, Direct Testimony of Linda Bridwell, Tables 1 and 2.

Maximum Day Demand (for normal weather) are, approximately, 12.06 mgd for year 2020 and 81.67 mgd for year 2030.⁵⁷ These incremental treatment capacity needs are under an assumption that KAWC's "base" treatment capacity for these years is 65 mgd.

The expectation is that the project will be substantially complete in year 2010.⁵⁸ It is unclear whether Kentucky-American's "rated capacity" will be 65 mgd or 70 mgd at that time.⁵⁹ Thus, in 2010, Kentucky-American Water Company's additional treatment capacity need ranges from between .87 mgd⁶⁰ and 10.33 mgd.⁶¹ While an argument that the project could result in an excess of capacity in the early years, the test is not whether there could be an excess at the instant the project goes into service.

The test is whether there will be an excess of capacity relative to the needs of the immediately foreseeable future, and, as noted, this period may embrace a number of years.⁶² Further, given that it is also possible that additional treatment capacity of approximately 10 mgd might be needed in year 2010, it does not appear that the project results in an unreasonable amount of additional capacity relative to need. The corresponding 42-inch transmission line appears within the

⁵⁷ Application, Direct Testimony of Linda Bridwell, Tables 1 and 2.

⁵⁸ See, for example, Application, Direct Testimony of Richard Svindland, page 15.

⁵⁹ Application, Direct Testimony of Linda Bridwell, page 30; KAWC Response to LFUCG Initial Request for Information, Item 4 of 7 (regarding temporary re-rating permit).

⁶⁰ Application, Direct Testimony of Linda Bridwell, Table 1 (Total Max Day Demand (normal weather) of 70.87 mgd minus 70 mgd rated capacity equals a .87 mgd treatment deficit.)

⁶¹ Application, Direct Testimony of Linda Bridwell, Table 1 (Total Max Day Demand (hot, dry scenario) of 75.33 mgd minus 65 mgd rated capacity equals a 10.33 mgd treatment deficit.)

⁶² *KU v. PSC*, 390 S.W.2d at 171.

range of reason for moving the water to central Kentucky.⁶³ The sizing of the project appears reasonable.⁶⁴

B. It is unclear whether the project will result in an excessive investment in relation to productivity or efficiency.

Per the Application, the estimated cost to construct the facilities is approximately \$160,000,000.⁶⁵ In terms of a recent update, the estimated construction cost (based on bids) is approximately \$155,857,000.⁶⁸ The estimated annual cost of operating the facilities is \$6,024,957.⁶⁹

Determining whether the proposal results in an excessive investment relative to productivity requires a comparison of the proposal to other reasonable alternatives for meeting the need. The question in simple terms: Is there a better way? There have been numerous studies, in several different forums,⁷⁰ of Kentucky-American Water Company's (and central Kentucky's) source of supply challenge. Several studies include consideration of Louisville Pipeline options.⁷¹ A pipeline interconnection of KAWC and LWC is a concept lending itself to use

⁶³ See TE Vol. II of III, page 69 (25 mgd through smaller line possible, but would require more energy and a different design); TE Vol. II of III, page 297 (42-inch line can handle 25 mgd and 30 mgd flow rates); TE Vol. II of III, pages 329 through 331 (appropriate size main from a surge transient standpoint).

⁶⁴ TE Vol. II of III, pages 314 and 315 (project allows room for possible expansion to 40 mgd).

⁶⁵ Application, page 6, Numbered Paragraph 12.

⁶⁸ KAWC Response to PSC 1 – 31, revised by update on 29 February 2008.

⁶⁹ Application, page 10, Numbered Paragraph 10.

⁷⁰ For example, "The Harza Study" for the Kentucky River Basin Steering Committee; the Kentucky Water Resources Research Institute study for the Kentucky River Authority; the Fayette County Water Supply Planning Council; the Lexington-Fayette Urban County Government; and the O'Brien and Gere study for the Bluegrass Water Supply Commission.

⁷¹ LWC did not conduct an extensive investigation or review of the water supply in central Kentucky. TE Vol. III of III, page 251.

as a measure of the reasonableness of the investment in relation to efficiency or productivity of KAWC's Pool 3 proposal. Nonetheless, there are caveats.

The primary concerns⁷² for any Louisville Pipeline option as a measure of the reasonableness of Kentucky-American's proposal relate to the lack of specificity on issues of route, participants, cost, and reliability. The concerns are not immaterial or academic points. As a prelude to discussing the concerns, however, a summary of the LWC concept is appropriate.

On 1 October 2007,⁷³ the LWC's Board of Water Works gave its President, Mr. Gregory Heitzman, authorization "to propose a 25 mgd supply of potable water to central Kentucky."⁷⁴ The Louisville Pipeline option includes: LWC construction and funding of a 36-inch transmission main from LWC facilities at English Station Road and I-265 in Jefferson County to Kentucky Highway 53 in Shelby County ("Section 1"); LWC collaboration "through public/private partnerships" in the construction and financing of a 36-inch transmission main from Kentucky Highway 53 in Shelby County to Kentucky-American Water Company's 24-inch water main at Newtown Pike in Fayette County; and corresponding pumping stations and storage facilities ("Section 2").⁷⁵

⁷² The Attorney General will not address every conceivable concern with the LWC plan. As with the Kentucky-American Water Company proposal, there are necessarily projections, estimates, and assumptions. Further, the Louisville Pipeline option remains a nascent concept. TE: Vol. III of III, page 284 (LWC has "conceptual scenarios.").

⁷³ It is not necessary to address directly the LWC 42-inch transmission main option; additionally, a scenario under which LWC has ownership of the pipeline to the delivery point at the intersection of Newtown Pike and Iron Works Pike is not proposed and has not been studied by LWC (TE Vol. III of III, page 283).

⁷⁴ Prefiled Rebuttal Testimony of Gregory C. Heitzman, 1 October 2007.

⁷⁵ Prefiled Rebuttal Testimony of Gregory C. Heitzman, 1 October 2007.

Subsequent to this authorization, there have been numerous revisions and modifications to the concept. One revision following the November 2007 hearing is that LWC has made clear a stronger intent to extend facilities to Frankfort, Kentucky with regard to Section 2 of the plan.⁷⁶ An additional revision is the suggestion of interim measures that could be taken in tandem with Louisville Water Company's efforts for a long-term solution.⁷⁷

Yet, with these revisions, the exact route of the pipeline is unknown.⁷⁸ Certainly for the route east of Frankfort, this raises questions of opposition. If the Louisville Pipeline option includes a segment through which the facilities of the Frankfort Plant Board are utilized, then this route raises material, fundamental questions relating to hydraulics that have not been studied.⁷⁹ Implicit in the concept of a reasonable alternative solution is a reasonable basis to conclude that it would work.⁸⁰ Even if the Frankfort Plant Board facilities are not utilized, the route issue still presents material, fundamental questions relating to implementation.⁸¹

Moreover, part of the allure of a Louisville Pipeline option is the suggestion that existing rights-of-way could be used for locating the facilities (thereby reducing inconvenience to the public). As the case has proceeded, the

⁷⁶ VR 3/05/08; 11:22:55 to 11:23:25 and 11:54:57 to 11:55:37; but see VR 3/05/08; 11:58:09 to 11:59:40 (LWC intends to create a partnership for segment between Shelbyville to Frankfort.); 12:00:30 to 12:02:04 (no signed agreement for partnership between LWC and potential partners).

⁷⁷ VR 3/05/08; 11:07:04 to 11:07:38.

⁷⁸ VR 3/05/08 11:27:28; LWC Response to OAG 1 – 3 (A final route selection has not been made.); TE Vol. II of III, page 177; TE Vol. III of III, page 284 (LWC has not performed a route analysis between Hwy 53 and Newton Pike.)

⁷⁹ For a listing, see Rebuttal Testimony of Richard Svindland, pages 6 and 7.

⁸⁰ Thus, questions concerning route and reliability converge on this point.

⁸¹ See Rebuttal Testimony of Linda Bridwell, pages 5 to 7.

ability to utilize rights-of-way has been subject to a significant amount of revision such that the initial notion of using I-64 itself as a pathway⁸² is now a concept of locating a project along the I-64 corridor.⁸³ The actual plausibility of locating facilities in existing rights-of-way, which necessarily has a significant impact on costs and the ability to implement the project in a timely fashion, does not share the same certainty as the attractiveness of the idea.

There are also significant issues relating to participation (and, in turn, costs). Louisville Pipeline contemplates a public/private partnership. To be clear, regionalization and cooperation (including public/private partnerships) are laudable and, perhaps, soon to become indispensable in water issues.⁸⁴ However, the identification of the party who will build, operate, and own facilities to carry water from Frankfort to Lexington remains unknown.⁸⁵ Further, the sizing for the pipeline remains unknown.⁸⁶

Louisville Water Company notes that it cannot do the project by itself.⁸⁷ The Commission should proceed with great caution in utilizing an alternative

⁸² See, for example, LWC response to OAG 1 – 7 (b) (“The Louisville Pipeline alternative includes installation of a 42 mile 36-inch pipeline adjacent to or within the existing I-64 right-of-way (from Kentucky Highway 53 to Newtown Pike).

⁸³ LWC response to KAWC 1 – 68 (Rectenwald e-mail to Heitzman, “In sum, it became apparent that for KTC long, parallel encroachments were a logical construct only, and only in the most dire circumstance and only for extremely short distances would they ever consider the possibility of a parallel line of their right of way.”); see, for comparison, TE Vol. II of III, pages 87, 88; KAWC response to hearing data requests, Item 3 of 15 (a significant amount of private easements were anticipated for each Louisville Pipeline route); TE Vol. III of III pages 190 through 196); TE Vol. III of III, pages 287, 288, and 290 (LWC is recommending an I-64 “corridor route.”); TE Vol. III of III, page 317.

⁸⁴ And, to be equally clear, the Louisville Water Company has a valuable role in addressing water issues in the Commonwealth.

⁸⁵ VR 3/05/08; 11:26:15 to 11:27:24.

⁸⁶ VR 3/05/08; 11:56:45 to 11:58:07.

⁸⁷ VR 3/05/08; 11:27:18 to 11:27:45.

that does not provide a clear view of participants who are necessary to support the alternative or their terms of participation including any ownership percentages.⁸⁸ Facts regarding participation are necessary to determine the threshold question of economic feasibility; likewise, facts regarding participation in a Louisville Pipeline project go to the heart of the question of investment versus efficiency and productivity.

Finally, reliability is an issue. The most startling revelation of the various hearings (and of the past decade) is the testimony that a 36-inch pipeline would not work.⁸⁹ Again, implicit in measuring the efficiency and productivity of Kentucky-American's Pool 3 option is a belief that the corresponding alternative would also solve the problem.

The above assessments of the Louisville Pipeline option are not to suggest that the option could never work (or that it is *per se* unreasonable). The above assessments are to point out that the **Louisville Pipeline proposal is only a means to assist the Commission** in testing the reasonableness of Kentucky-American Water Company's proposal, and there are caveats to its use for that function.⁹⁰

⁸⁸ One way to consider this problem is to compare the lack of clearly identified participants for a pipeline project with a lack of a clearly identified "consumer market." See also TE Vol. III of III, pages 312 through 314 (rather than 80/20, perhaps it will be 1/3rd, 1/3rd, 1/3rd).

⁸⁹ TE Vol. III of III, page 98 (KAWC: "36-inch pipe would blow crossing the river, crossing the Kentucky River"). This is in stark contrast to KAWC's prior representation that there were no "technical, engineering or legal impediments" to the Louisville Water Company option. KAWC response to CAWS First Supplement Data Request, Item 9 of 19 (b).

⁹⁰ The Commission expressly notes the role of LWC. LWC is a participant in order to "assist the Commission in developing facts and issues." Order, 26 November 2007, footnote 1.

The above notwithstanding, the Louisville Pipeline option offers the following information to this proceeding.⁹¹ The Louisville Pipeline option corresponds to lower capital construction costs.⁹² On a per unit basis, the non-capital cost of water under the Louisville Pipeline option is higher.⁹³ At relatively low levels of usage, the net present value of the Louisville Pipeline option is roughly the same as the net present value of the Kentucky-American Water Company Pool 3 project.⁹⁴ For projections of higher levels of usage, the net present value of the KAWC Pool 3 project is lower than the LWC option.⁹⁵

In a “best case” scenario in favor of the Louisville Pipeline option, the evidence leads to the conclusion that the Kentucky-American Water Company’s proposal is generally comparable to LWC’s option.⁹⁶ Both can be reasonable.⁹⁷ Nevertheless, it is Kentucky-American’s burden to demonstrate the **absence** of wasteful duplication. KAWC’s proposal does not satisfy this burden.

⁹¹ In determining the Net Present Value of the Louisville Pipeline, the Attorney General gives consideration to all the evidence in the record. The Attorney General does not accept the R W Beck reports as conclusive.

⁹² TE Vol. II of III, page 252.

⁹³ TE Vol. II of III, page 252.

⁹⁴ TE Vol. II of III, pages 175 and 254 (Net Present Value of Pool 3 Option (per AG) is approximately \$273.0 million, estimate of Net Present Value of Louisville Pipeline ranges between \$255.0 and \$277.0 million); TE Vol. II of III, page 212 (Costs of proposal and alternative are essentially the same.); TE Vol. II of III, pages 252 and 253; compare with TE Vol. III of III, pages 64, 65, and 76 (KAWC: Pool 3 approximately \$51.0 million less expensive than Louisville proposal for 42-inch pipeline comparison).

⁹⁵ TE Vol. II of III, page 252.

⁹⁶ TE Vol. II of III, page 207 (Rubin: KAWC proposal appears to be reasonable.)

⁹⁷ TE Vol. II of III, page 268; also see TE Vol. III of III, page 252 (LWC does not take the position that the KAWC proposal will not work), and TE Vol. III of III, pages 324 and 325 (In November 2007, LWC indicated that KAWC proposal is a reasonable alternative).

In order to meet the test of reasonableness (and to demonstrate an absence of wasteful duplication by minimizing the investment in relation to productivity and efficiency), three conditions are necessary.

Condition No. 1 – Conservation Program

Kentucky-American Water Company should be required to hire a qualified conservation consultant to develop a conservation program consistent with best practices in the water industry.⁹⁸ KAWC accepts this condition.⁹⁹ The Attorney General further notes that this is not a request for window dressing. It is a request for KAWC to finally address a long-standing concern.

From PSC Case No. 9283:¹⁰⁰

The record in this case indicates that Kentucky-American considers water conservation techniques to be an option available only to its customers. Kentucky-American has not incorporated programs to reduce demand into its system planning, nor implemented an aggressive program to encourage the efficient use of water. Mr. Edens stated, "as related to conservation, I think the efficiency simply comes for the utilization of the product by the customer." Exhibits provided during the hearing indicate Kentucky-American has prepared a certain amount of literature on techniques to reduce water consumption.

Testimony presented by Mr. Edens during the hearing indicates that unless there is a supply problem, management is not particularly interested in water conservation programs. According to Mr. Edens, the conservation concept "is addressed only when there is a source of supply situation and that is not the case at Kentucky-American Water Company." He also stated that "until such time as

⁹⁸ See, generally, Rubin Pre-filed Testimony, pages 4, 18, and 19; TE Vol. II of III, page 261 (goal is reduce both end-use consumption and loss of water on utility's side of the meter).

⁹⁹ KAWC Rebuttal Testimony of Linda Bridwell, page 9; TE Vol. I of III, page 128.

¹⁰⁰ *In the Matter of: Notice of Adjustment of the Rates of Kentucky-American Water Company*, Case No. 9283, Order, October 1985, page 44.

there is a source of supply problem the conservation issue, up until now, has not been applicable to Kentucky-American. [footnotes omitted]

The irony is that KAWC's position, as noted by this Commission, reflects Kentucky-American's philosophy on conservation at approximately the same point in time that a management audit identified KAWC's current source of supply drought risk. Over two decades later, Kentucky-American's attitude toward conservation (reducing end-use and water loss on KAWC's side of the meter) remains open to question and criticism.¹⁰¹ The Attorney General requests that the Commission establish a separate docket on this matter.

The Attorney General's condition on conservation is a call to action that is necessary for this project to be in the public interest. In order to protect the public interest, there must be a mechanism in place whereby Kentucky-American is accountable for its efforts in furtherance of this commitment (and penalized for any failure to comply).

Condition No. 2 – Water Supply and Demand Management Plan

Kentucky-American Water Company should be required to file with the Commission a new water supply and demand management plan within six months of the date on which utilization of the new plant reaches 80% of capacity for one day (unless such utilization is the result of a temporary outage at

¹⁰¹ The Commission may take administrative notice of RWE's concerns about non-revenue water in the American system; further, the current record is replete with concerns as to why Kentucky-American is not doing everything it can to reduce its need for water.

KAWC's Richmond Road Station, or other short-term emergency such as a serious fire).¹⁰² KAWC accepts this condition.¹⁰³

Condition No. 3 – Cost Cap

Finally, to conclude that the Pool 3 Project is the reasonable, least-cost solution for Kentucky-American Water Company, the Commission must impose a condition that limits the costs that KAWC can recover through its rates.¹⁰⁴ The testimony of his witness, Scott J. Rubin, uses the term "retail rates" when discussing the cap. The Attorney General notes that his recommendation is for a cap that limits the costs that KAWC can recover through its rates that are subject to the jurisdiction of this Commission. Thus, KAWC's sales for resale also fall under the recommended cap. Kentucky-American does not does accept this condition.¹⁰⁵ For the Attorney General, this is a "deal-breaker."

The Commission may, as a condition for granting a CPCN for the proposed facilities, limit the amount that Kentucky-American may include in its rate base for ratemaking purposes to the estimated cost of the proposed facilities at the time a CPCN is issued.¹⁰⁶ In order for the record to provide adequate evidence of the absence of wasteful duplication, a cost cap is necessary.

KRS 278.020 requires Kentucky-American to obtain approval for this project. While the legislature prohibits the Commission from refusing or

¹⁰² See, generally, Rubin Pre-filed Testimony pages 4, 19, and 20.

¹⁰³ Rebuttal Testimony, Linda Bridwell, page 10; TE Vol. I of III, page 129.

¹⁰⁴ See, generally, Rubin Pre-filed Testimony, pages 4, 17, and 18.

¹⁰⁵ TE Vol. I of III, pages 127 and 128.

¹⁰⁶ The Attorney General provides his answer to Question No. 4 of Appendix E of the Commission's 21 December 2007 Order. The Attorney General's answers to Question Numbers 1, 2, and 3 appear in a separate appendix item (Appendix Item A) to this Brief.

modifying a certificate application under KRS 278.023 without the consent of the parties to the agreement,¹⁰⁷ that prohibition does not apply to Kentucky-American's pending application. Hence, Kentucky-American does not have any right to build this facility nor may it demand unconditional acceptance of its application. Just as this Commission has, in numerous instances, conditioned authorization under KRS 278.020 for a change in control,¹⁰⁸ it may likewise condition the approval of the pending certificate application in order to protect the public interest.

KAWC has the burden of proof on each element of the test for obtaining approval. It must demonstrate the absence of wasteful duplication as a condition of receiving authorization. It is a determination made "up-front." In furtherance of its Application, Kentucky-American presents its financial projections including construction costs. Kentucky-American has an opportunity to earn a reasonable return on its investment, and it is quite difficult to discern any unfairness or lack of opportunity through holding Kentucky-American to its own factual representations to this Commission. In other words, because Kentucky-American presents these capital cost projections for the Commission to rely upon, the Commission has full authority to require Kentucky-American to stand behind its own numbers.

While Kentucky-American may argue, "let us build it, and we can take care of any problems later," such a position is not in the public interest. A

¹⁰⁷ KRS 278.020(1).

¹⁰⁸ Including application involving the Kentucky-American Water Company, see, for example, Case Numbers 2002-00018, 2002-00317, and 2006-00197.

decade ago, Kentucky-American began work on a 36-inch pipeline interconnection with the Louisville Water Company. Presumably, the very first technical question to address: Will it work? Now, a decade later, for the first time, Kentucky-American Water Company reveals that a "36-inch pipe would blow crossing the river, crossing the Kentucky River."¹⁰⁹ There will be no solace if Kentucky-American is as off-the-mark on its financial projections for the Kentucky River project.

The framework for determining the absence of wasteful duplication under KRS 278.020 is not for Kentucky-American to do something now and pour through the results later. The intent of the certificate requirement is to ascertain the absence of wasteful duplication now. If Kentucky-American wants such a conclusion based upon its numbers, then the Commission must require KAWC to stand behind them.¹¹⁰

Given that Kentucky-American has not met its burden on the issue of economic feasibility, a cost cap is equally important for that issue as well. The question of economic feasibility is not a matter to resolve *ex post* in a rate proceeding. Again, the certificate proceeding is a measure to prevent a project that is not economically feasible. Therefore, a cost cap is a necessary measure to protect the ratepayers and the public interest.

¹⁰⁹ TE Vol. III of III, page 98.

¹¹⁰ Whatever regulatory doomsday scenarios Kentucky-American may suggest, the Attorney General notes that the Commission has the power to revisit any Order should a regulatory condition, such as this one, compromise the utility's ability to continue to provide service or cause a legitimate constitutional or statutory concern. Otherwise stated, if there is an extraordinary event or set of circumstances, the Commission's hands will not be irrevocably tied through such a condition.

If the Public Service Commission conditions the approval of the Kentucky-American Water Company plan on the acceptance of a cost cap, then the record could provide adequate protection on the issue of economic feasibility and adequate evidence of the absence of wasteful duplication. Otherwise, the Commission should not approve the Application.

- C. The project does not appear to result in an unnecessary multiplicity of physical properties, such as right of ways, poles and wires.

In order to determine an absence of wasteful duplication, the Commission also must make an assessment regarding the multiplicity of physical properties. Minimization of physical properties can help to minimize the investment in facilities, and it tends to reduce inconvenience to the public.

We think that "duplication" also embraces the meaning of an excessive investment in relation to productivity or efficiency, and an unnecessary multiplicity of physical properties, such as right of ways, poles and wires.¹¹¹

Judicial precedent indicates that the Commission should consider whether it is feasible to use existing transmission facilities when considering an application for new transmission facilities.¹¹² If it is not feasible to use existing transmission facilities, then the Commission is justified in granting a certificate to meet an identified need.¹¹³

In order to gain access to additional supply, Kentucky-American is going to Pool 3 on the Kentucky River. The weight of the evidence does not suggest a

¹¹¹ *KU v. PSC*, 252 S.W.2d at 890. This latter aspect includes "economic loss through interference with normal uses of land, that may result from multiple sets of right of ways, and a cluttering of the land with wires and poles." *KU v. PSC*, 252 S.W.2d at 892.

¹¹² *Kentucky Utilities Company v. Public Service Commission*, 252 S.W.2d 885, 892 (Ky. 1952).

¹¹³ *KU v. PSC*, 252, S.W.2d at 892.

closer location for access to sufficient additional water supply (and, in turn, sufficient amounts of treated water). From the site of the Pool 3 Project to the inter-connection with KAWC's central Kentucky distribution system, there does not appear to be a comparable (or otherwise adequate) existing treatment facility or transmission facility that the 42-inch transmission main will duplicate. For this aspect of the test regarding wasteful duplication (of physical properties), that question, essentially, exhausts the inquiry. For this element, there is no wasteful duplication through the proposed facility or transmission main.

There is advocacy for the proposition that the Commission must take into account Louisville Water Company's excess treatment plant capacity. The position appears to be that it is wasteful duplication (**in terms of additional physical properties, right-of-ways, etc.**) to approve a KAWC project for new treatment capacity while LWC presently has excess capacity. In this sense, there is advocacy that the utilization of LWC's excess plant capacity has a "priority" in order to prevent wasteful duplication of KAWC physical properties.

While it is appropriate to consider a Louisville Water Company alternative, the Legislature has not assigned the Commission the regulatory control over the Louisville Water Company's construction activities and LWC's creation of physical properties. Thus, while the Commission may take LWC's excess plant capacity into consideration in terms of LWC's ability to serve, it does not follow that the Commission must necessarily seek to exhaust the excess

capacity of non-jurisdictional utilities as a requirement in order to curtail additional physical properties of a jurisdictional utility.¹¹⁴

Finally, there is advocacy that the Louisville Pipeline will be built; therefore, eventually, there will be an undue multiplicity of physical properties. The primary concern with such an argument is the significant amount of speculation on this point. If Louisville Water Company currently had a transmission facility in operation, then, under *Kentucky Utilities Co. v. Public Service Commission*, 252 S.W.2d 885, 891, 892 (Ky. 1952), harmful duplication of physical properties might result such that the Commission would have to make determinations regarding the use of the facility and the absence of wasteful duplication. Such a facility does not exist.

Arguably, if Louisville Water Company had a specific plan underway and close to completion, then the use of an imminent facility is likewise directly relevant. However, right now, there is only speculation that a LWC facility will be built, and the capacity of the facility is unknown. The threat of multiplicity of physical properties that result from a possible LWC project is just conjecture.

¹¹⁴ KRS 278.020 does not contain such an instruction. *Kentucky Utilities Co. v. Public Service Commission*, 252 S.W.2d 885 (Ky. 1952) does not suggest such a result.

3. Additional Considerations

Opposition

It is well-documented that there was significant opposition to Kentucky-American Water Company's plan to inter-connect with the Louisville Water Company roughly a decade ago. Likewise, it is clear that there is significant opposition to Kentucky-American's current plan. The record reflects that, regardless of alternative, a project may entail the acquisition of private easements from a significant number of property owners as well as other interruptions. For this reason (as well as others, such as concerns about the environment, etc.), it is reasonable to expect continuing opposition to any option.¹¹⁵

The Commission is not precluded from conducting an examination into the opposition to a project. Nonetheless, following a review of the statutes, case law, and Commission precedent, one point is manifest. The Commission's powers are purely statutory, and "it cannot decide issues not subject to its jurisdiction."¹¹⁶ Thus, KRS 278.020 does not invest the Commission with authority to determine all issues relating to a project.¹¹⁷

For those matters that are not subject to the Commission's authority, there are other forums for resolving those matters. If the Commission grants a

¹¹⁵ TE Vol. III of III, page 257 (LWC cannot guarantee that there would be no opposition to its proposal.)

¹¹⁶ See, for example, *In the Matter of: The Application of East Kentucky Power Cooperative, Inc. For a Certificate of Public Convenience and Necessity to Construct a 161 KV Transmission Line in Barren, Warren, Butler, and Ohio Counties*, Case No. 2005-00207, Order, 31 October 2005 (Federal laws such as the National Historic Preservation Act and the National Environmental Policy Act are not within the Commission's jurisdiction.)

¹¹⁷ See, for comparison, Case No. 2005-00207 (full citation above), Order, 31 October 2005 ("The appropriate procedure is for the Commission to issue rulings based on a consideration of only those issues over which it has jurisdiction.")

certificate, then it falls to Kentucky-American to address all remaining matters and determine how to proceed to resolve any conflicts or problems.

Kentucky River Authority and the Kentucky Division of Water

The Kentucky River Authority has the responsibility for long-range water resource and drought response planning for the Kentucky River Basin.¹¹⁸ The KRA coordinates the Kentucky River Basin resources activities among state agencies.¹¹⁹ During its 25 May 2007 meeting, the KRA approved a Resolution endorsing the use of Kentucky River Pool 3 as a regional water source.¹²⁰ While the KRA endorsement does not bind the Commission, the policy determination of the agency acting within its water resource planning authority for the Kentucky River Basin does reflect the public policy of the Commonwealth.

There have been questions about the adequacy of water available in Pool 3. The Kentucky Division of Water issued Water Withdrawal Permit #1572 to the Kentucky-American Water Company. DOW has made the determination that adequate water is available for the Pool 3 project, and the Attorney General is not aware of any direct challenge to DOW's determination.¹²¹ This proceeding is not a forum for a collateral attack upon the permit.

¹¹⁸ KRS 151.720 (Powers of authority).

¹¹⁹ KRS 151.720(15).

¹²⁰ See 6 June 2007 letter from Stephen Reeder, Executive Director of the KRA, to Beth O'Donnell.

¹²¹ See also KAWC Response to CAWS First Data Request, Item 1, 10 April 2007 Division of Water letter regarding Permit #1572; TE Vol. II of III, pages 66, 67, 336 through 343 (Pool 3 can provide 25 mgd without restriction and, perhaps, up to 40 mgd without restriction).

Bluegrass Water Supply Commission

While Kentucky-American Water Company's application is for approval of a 20 mgd water treatment facility, KAWC made a decision to incorporate into the design an additional 5 mgd capacity module for the express purpose of providing this capacity for the Bluegrass Water Supply Commission.¹²² In sum, BWSC is an entity that includes the Lexington-Fayette Urban County Government and several municipal water utilities that are close in proximity to KAWC. While the exact nature of BWSC's participation in this project remains to be seen,¹²³ the 5 mgd capacity increment corresponds to a multi-party regional water supply/treatment initiative. The Attorney General's recommendation is not contingent upon the participation of BWSC.

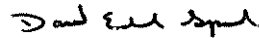
¹²² Application, pages 6, 7, Numbered Paragraph 13; Exhibit A – Specifications Volume III, page 1; Exhibit A – Specifications Volume IV.

¹²³ TE Vol. III, page 351.

WHEREFORE, the Attorney General tenders his Brief and prays that this Commission conditions its approval of the Kentucky-American Water Company upon the acceptance of a cost cap by the Applicant¹²⁴.

Respectfully submitted,

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¹²⁴ The Commission should place two additional conditions, a conservation program and water supply and demand management plan, which the company has accepted in this proceeding.

Notice of Filing and Certificate of Service

Counsel gives notice that the original and eight photocopies of the Attorney General's Brief were filed by hand delivery to Beth O'Donnell, Executive Director, Public Service Commission, 211 Sower Boulevard, Frankfort, Kentucky 40601. Counsel also certifies service of this document by mailing a true and correct photocopy of the same, first class postage prepaid, to the parties of record. Filing and service took place this 20th day of March, 2008.

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Appendix

Response by the Attorney General to the Commission's 21 December 2007 Order
Requesting Information, Questions 1, 2, and 3.

Response by the Attorney General to the Commission's
21 December 2007 Order Requesting Information

Preliminary Statement Regarding Responses

The Commission is conducting a comprehensive review of Kentucky-American Water Company's application for a certificate of convenience and necessity. Through a 21 December 2007 Order, the Commission provides four questions for each party to address in its brief. The Attorney General provides his responses to three of these questions through a separate part of his Brief.

Question Numbers 1, 2, and 3 of the December 21st Order's Appendix E do not seek the application of law to a specific set of facts or small number of factual scenarios. These questions ask "is it conceptually possible" rather than is a specific plan or course of action lawful.

It is not practical (or perhaps even possible) to address every possible factual scenario for each question. Also, with history as a guide, cases such as *City of Olive Hill v. Public Service Commission*, 305 Ky. 249, 203 S.W.2d 68 (Ky. 1947) and *McClellan v. Louisville Water Company*, 351 S.W.2d 197 (Ky. 1961), readily demonstrate that such legal questions (even under a specific set of facts) are difficult to resolve (and pronounce as "well-settled"). The Attorney General can only offer his assessment of how the Judiciary would **approach** each issue.

1. Does the Louisville Water Company have the legal authority to make wholesale water sales in the counties other than Jefferson County and those counties that are contiguous to Jefferson County?

Response:

The Attorney General reads Question Numbers 1 and 2 in tandem such that this question seeks an understanding of the Louisville Water Company's authority to engage in wholesale water sales in scenarios in which LWC does not construct, own, or operate a transmission main outside of the outer boundaries of those counties that are contiguous to Jefferson County. (Otherwise stated, LWC's point of delivery for the wholesale service is not outside the outer boundaries of those counties that are contiguous to Jefferson County.)

Yes, (the Judiciary would conclude that) LWC water **could** lawfully flow past the outer boundaries of those counties contiguous to Jefferson County. See, for example of general principle, *Dyer v. City of Newport*, 123 Ky. 203, 94 S.W. 25, 26 (Ky. 1906)(a municipal water company has the authority to sell water to "outsiders" - persons located outside the city's corporate limits). Nevertheless, the Attorney General notes that LWC does not have unconditional authority. For example, through KRS 151.200, a transfer into a watershed requires a permit. For counties in the Kentucky River Basin, the issuance of such a permit is subject to the jurisdiction of the Kentucky River Authority.¹

¹ See KRS 151.729 (Authority's involvement in requested transfer of drinking water between water utilities involving Kentucky River basin watershed); also see KRS 151.720(15)(KRA coordinates Kentucky River basin water resources activities among state agencies); and KRS 224.70-140(In part: permits issued pursuant to KRS Chapter 151 shall be consistent with administrative regulations of KRA and long-range water resource plan and drought response plans developed by KRA).

2. Does the Louisville Water Company have 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?

Response:

(The Judiciary would likely conclude the following.) The General Assembly controls the territorial limits for each municipal water supplier. KRS Chapter 96 provides two territorial limits.

KRS 96.150 contains a general rule for extra-territorial municipal water and sewer service. Per KRS 96.150, the utility may construct, own, and operate a system in “any territory contiguous to the city.”

KRS 96.265 sets for a specific rule (which prevails over the general rule), and the Louisville Water Company falls within the scope of KRS 96.265 rather than KRS 96.150. Per KRS 96.265: LWC is without authority to extend its system beyond the counties that are contiguous to Jefferson County. Thus, LWC may not “unilaterally” extend (construct, own, and operate) a water supply facility into, for example, Franklin County **in anticipation** of a future wholesale arrangement. Nevertheless, there are additional statutes in KRS Chapter 96 addressing extra-territorial service as well as additional sources of authority.

While KRS 96.265 contains a territorial limit, it is important to note that a Court could reasonably conclude that the territorial limits of both KRS 96.150 as well as KRS 96.265 apply only to a municipal utility’s provision of retail water service. A Court **would likely** seek to harmonize the foregoing territorial

limitations with the express authority for extra-territorial operations under KRS 96.120, KRS 96.130, and KRS 96.140 (and other possible statutory authorizations such as the ability to act jointly through an interlocal agreement). The Attorney General does not believe that it is the intent of the legislature (through KRS 96.265) to prohibit any extra-territorial expansion of LWC's system.

Hence, while LWC acting on its own does not appear to have the statutory authority to construct, own, and operate a water transmission main for possible wholesale water service to entities outside of the territorial limit of KRS 96.265, there is at least one instance - an interlocal agreement - through which LWC **could** identify statutory authority for the construction, ownership, and operation of a water transmission main for such a purpose.

It is not possible to address all the various factual and legal scenarios that are possible under this question (or even possible through the example of an interlocal agreement). Such a discussion, however, is not necessary. It is enough to convey that the Attorney General believes that the Judiciary **would likely** determine the existence of a statutory basis through which LWC **could** extend its system to provide extra-territorial service in at least one situation.

Again, as with the response to Question Number 1, there are also conditions to LWC's ability to extend its system. For example, an interlocal agreement would have to meet the requirements of KRS Chapter 65.210 *et seq.* Additionally, the project would also be subject to legal requirements of KRS Chapter 151 (and the jurisdictional power of the Kentucky River Authority).

3. Does the LFUCG have the statutory authority to construct, own and operate a joint public-private venture to supply water to Kentucky-American and any other regional water suppliers?

The phrases “public-private partnership” and “public-private venture” both refer to an umbrella concept that describes **any** collaboration between public and private entities. For example, the distribution of government publications by private retail establishments is a public-private coordination of effort. Further, an arrangement through which a government leases property to a private entity meets the definition of a public-private partnership as does a contract through which a government delivers a service through or with a private entity.² It is not practical to address the LFUCG’s statutory authority to enter into such a broad array of potential arrangements under the generic definition of a “public-private venture.” There are simply too many legal and factual variables. Nonetheless, the Attorney General offers the following.

“The Lexington-Fayette Urban County Government is a creature of the General Assembly,” and it “possesses only those powers granted by the General Assembly.”³ Per KRS 67A.060, LFUCG can exercise the constitutional and statutory powers of counties and cities of the highest class within the county.⁴

A city of the second class may engage in the provision of water service.⁵ Whatever rights and responsibilities that KAWC has regarding its ability to provide water service to Fayette County, the Attorney General does not believe

² See, for examples applicable to KAWC, KAWC Responses to PSC Post-Hearing Data Requests, Item 5.

³ *Goodloe v. Baesler*, 539 S.W.2d 298, 300 (Ky. 1976).

⁴ Per KRS 81.010 (2), Lexington is a city of the second class.

⁵ KRS 96.355

that a Court would conclude that the grant of a franchise to KAWC by the Lexington-Fayette Urban County Government precludes LFUCG from participating in projects (or ventures) relating to water supply. Put another way, it is reasonable to suggest that the Judiciary would recognize KRS 96.355 as an adequate basis of statutory authority for LFUCG to participate in a public-private venture with the Kentucky-American Water Company and any other regional water supplier (with the latter participating through, say, an interlocal agreement).

The LFUCG's authority, however, does have conditions. Foremost, the LFUCG's expenditure of money must be for a project with a valid public purpose.⁶ Further, any venture would also have to comply with constitutional and statutory provisions including limits regarding the ownership of property, the extension of credit, and regulatory permitting requirements.

With the disclaimer that there is no specific plan or proposal for review, the Attorney General notes his belief that the Judiciary **would likely** hold that KRS 96.355 provides statutory authority for the LFUCG to construct, own, and operate a joint public-private venture to supply water to Kentucky-American Water Company and any other regional water suppliers. Thus, LFUCG **could** enter into an arrangement; however, it does not follow that all such forms of a venture would be lawful (or otherwise permissible).

⁶ See, for example, *Dannheiser v. City of Henderson*, 4 S.W.3d 542 (Ky. 1999).