

COMMONWEALTH OF KENTUCKY

RECEIVED

BEFORE THE PUBLIC SERVICE COMMISSION

AUG 13 2007

PUBLIC SERVICE COMMISSION

In the Matter of:

EXAMINATION OF THE OPERATION AND )  
REASONABLENESS OF THE OFFSETTING ) CASE NO. 2006-00191  
IMPROVEMENT CHARGE OF HENRY COUNTY )  
WATER DISTRICT NO. 2 )

VERIFICATION OF TESTIMONY OF THOMAS GREEN

Comes Thomas Green, of the engineering firm Tetra Tech, Inc., engineers for the Henry County Water District No. 2. (hereinafter "Henry District"), after first being duly sworn and states that he personally prepared the attached testimony in the above captioned matter, that he adopts same as his sworn testimony in this matter and that he verifies its authenticity.

Witness the hand of the undersigned this 9 day of August, 2007.

Thomas Green  
Thomas Green  
Tetra Tech, Inc.

STATE OF KENTUCKY )  
COUNTY OF Fayette )

The foregoing VERIFICATION OF TESTIMONY was acknowledged and sworn to before me this 9<sup>th</sup> day of August, 2007, by Thomas Green, Tetra Tech, Inc, engineers for Henry County Water District #2.

My commission expires: MY COMMISSION EXPIRES MAY 21, 2008

Lara Bentley  
NOTARY PUBLIC, KY. STATE AT LARGE

CERTIFICATE OF SERVICE

I certify that prior to the filing of the foregoing a true copy was this 13 day of August, 2007, mailed to:

Hon. David Edward Spenard  
Assistant Attorney General  
Office of the Attorney General  
Utility & Rate Intervention Division  
1024 Capital Center Drive, Suite 200  
Frankfort, Kentucky 40601-8204

A handwritten signature in black ink, appearing to read 'D. Berry Baxter', written over a horizontal line.

D. Berry Baxter  
Counsel for Henry District

1    PREFILED TESTIMONY OF

2    THOMAS GREEN

3

4    **Q. WHAT IS YOUR NAME AND BUSINESS ADDRESS?**

5    A. My name is Thomas Green. My business address is 800 Corporate Drive, Lexington,  
6    Kentucky, 40503.

7

8    **Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR POSITION?**

9    A. I am employed by Tetra Tech as a Senior Engineering Technician. We are the  
10   consulting engineers for Henry County Water District No. 2.

11

12   **Q.WHAT IS YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE?**

13   A. I am a high school graduate and I attended the University of Kentucky for two years.  
14   I have worked for Lexington consulting engineering firms since 1976. I began working  
15   in the capacity of surveyor and in 1984 I became registered. In 1982 I began learning the  
16   KYPipe hydraulic modeling program, first from the engineers at work and then by  
17   attending training classes given by the program's developers in the Engineering  
18   department at UK. I have continued to take these classes regularly over the years as the  
19   software has been upgraded. I have built hydraulic models of numerous water  
20   distribution systems in Kentucky, and I am experienced in other aspects of water work  
21   such as plan preparation and submittal, cost estimates, construction inspection, and  
22   easements. My experience also includes having developed the OIC methodology and  
23   worked for its approval.

1 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE A RATE REGULATORY**  
2 **BODY?**

3 A. I have not.

4

5 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

6 A. The purpose of my testimony is to discuss the origin and development of the Henry  
7 District's Offsetting Improvement Charge, the process by which it first gained approval,  
8 the regulatory guidelines which support it, the nature of its second review in the current  
9 Case 2006-00191, and the issues and concepts that are pertinent to its reasonableness. I  
10 would like to make my responses to previous interrogatories in this case part of my  
11 testimony by reference.

12

13 **Q. TO START, DO YOU HAVE ANY GENERAL OBERVATIONS?**

14 A. In Kentucky "SDC" is a relatively new term, but it does not create any new charges.  
15 The costs of system development already exist in districts across Kentucky, and these  
16 charges are already being paid every month within general rates. An SDC only changes  
17 who pays for these growth-necessitated costs. It assigns a reasonable share of that  
18 expense to growth and removes the unreasonable share of that expense from existing  
19 customers. Therefore, since SDCs make rates more reasonable, they are clearly in the  
20 public interest and would be actively supported by the Public Service Commission.

21

22 Henry District's position is simply that it is more reasonable to make this reallocation of  
23 costs than not to. Many complex questions have been posed by Commission staff during

1 the current investigation, and a great deal of detail will probably be covered in this  
2 hearing. But the essential question is not whether the OIC is a perfect calculation. It has  
3 been designed in good faith, its results are intentionally conservative, and we are  
4 confident that it is reasonable. We are also convinced that it is unreasonable for the  
5 District *not* to relieve its existing customers of a portion of the burden of growth-  
6 necessitated costs. Therefore the approval of the OIC ultimately depends not on its  
7 perfection, but on the greater fairness which it reasonably achieves.

8

9 **Q. WHAT WAS THE ORIGIN OF THE HENRY DISTRICT'S OFFSETTING**  
10 **IMPROVEMENT CHARGE?**

11 A. The policy in the Henry District was to sign a plat certification of service to a  
12 subdivision as long as the hydraulic capacity to serve new customers in that location that  
13 was adequate. I had developed the KYPipe computer model of the HCWD2 system  
14 which helped make these determinations. When capacity was inadequate, the developer  
15 or landowner would have to wait until the District's finances and manpower would  
16 permit them to construct a larger line before certifying water service.

17

18 In 1999 several developers who had proposed subdivisions along KY 146 west of New  
19 Castle combined to finance a larger water line because the district's existing line was  
20 inadequate to serve the increase in demand from their subdivisions. They did this  
21 voluntarily to expedite their projects after learning there would be a delay before the  
22 District could install a bigger line. The developers shared the cost of the project in  
23 proportion to their number of lots.

1 Shortly afterward another developer on a nearby road with good hydraulic capacity  
2 requested and quickly received approval for his development. One of the first group of  
3 developers phoned Don Heilman, then Chief Operating Officer, and said he understood  
4 why his group needed to pay to restore the capacity they took from the system, but why  
5 weren't all developers and new lots treated equally? He also made the point that twenty  
6 farmers who sold off single tracts were creating the same impact as a twenty lot  
7 subdivision.

8

9 Don took these comments seriously and decided to try to find a way to treat all  
10 developers and potential customers equally, and to require growth to pay its fair share,  
11 but no more. Don asked me to begin researching how to develop such a charge, so I  
12 made several calls and visits to the PSC in Frankfort, and that's how the process got  
13 started.

14

15 **Q. WHAT WERE YOU TOLD BY THE PSC?**

16 A. The staff was helpful and encouraging, but the only specific guidance they gave was  
17 to look into the tariff library to find similar charges. They mentioned North Shelby's  
18 Line Upsizing Charge, approved in 1995, but there were few other examples for us to  
19 follow. North Shelby's approach seemed less reasonable and comprehensive than what  
20 we wanted to do. So we used our own experience with the KYPipe model as the basis  
21 for a methodology incorporating specific offsetting improvements and costs to determine  
22 our charge.

23

1 **Q. WHAT WERE YOUR GOALS IN DESIGNING THE CHARGE?**

2 A. Beside the principle of fairness, we wanted to have a uniform charge per proposed  
3 residential unit systemwide. We knew that cost-based rates were generally considered  
4 preferable. We wanted to address the real needs of the district, and we wanted to be  
5 conservative in our calculations so that the situation of existing customers subsidizing  
6 growth was not reversed, but brought into a more reasonable balance.

7  
8 Our idea was simple: to compile a database of hydraulic improvement projects and the  
9 flow increase these larger lines could provide. We would divide the total cost of the  
10 projects by the total gallons-per-minute of flow increase to get the average cost per gpm  
11 of adding capacity to the distribution system. Based on Division of Water guidelines we  
12 would assign 1 gpm as the average residential peak demand. The average cost per gpm  
13 became the basis of the Offsetting Improvement Charge.

14  
15 **Q. DID YOU ASK FOR FEEDBACK FROM COMMISSION STAFF?**

16 A. Yes, and again they were helpful and encouraging. They said, of course, that they  
17 could not speak for the Commission, but that our approach seemed reasonable. However  
18 they said that until Administrative Case 375 on System Development Charges was  
19 complete, it would serve no purpose to submit our new tariff, because it could not be  
20 reviewed until after Case 375 was finalized. So we put the OIC project on hold. In the  
21 summer of 2001 we were discussing a related issue with Commission staff who told us it  
22 would then be appropriate to submit our OIC tariff.

23

1 **Q. WERE YOU TOLD THE OIC SHOULD BE MODIFIED IN ANY WAY PRIOR**  
2 **TO SUBMITTAL BECAUSE OF THE CASE 375 FINDINGS AND GUIDELINES?**

3 A. No. We had read the final order and SDC guidelines, and we were very encouraged  
4 that the Commission stressed flexibility and latitude for districts to design their own  
5 SDCs, going so far as to say “Because of the geographic and demographic diversity of  
6 the state and its water utilities, the use of rigid and inflexible standards for SDCs is not in  
7 the public interest.”

8  
9 The Attorney General’s written comments of October 24, 2000 in Case 375 strongly  
10 questioned the equity methodology, and also said that with incremental methodology, the  
11 “quandary” was the reasonableness of charging the new customer for all the  
12 infrastructure exclusively necessary to serve him, and then to charge that same customer  
13 general rates which contained costs related to system infrastructure not necessary to serve  
14 him. The difficulty we had in understanding how to quantify and remedy that situation  
15 was that the specific set of infrastructure elements not necessary to serve a new customer  
16 (and his consequent SDC adjustment) would be very different depending on the location  
17 of the new customer in the system. So we went to the other side of the scale and simply  
18 excluded from the OIC all the growth- necessitated costs for raw water supply, water  
19 treatment, pumping, and storage tanks. By limiting our charge to the distribution system  
20 we were addressing our most pressing and major need, and at the same time we were  
21 making a significant reduction to the OIC to be fair to the new customer.

22  
23 **Q. WHAT WAS THE OUTCOME OF CASE 2002-00393?**

1 A. The Commission gave us a three year approval, at which time said they would review  
2 the operation of the program. They said “the Commission agrees with Henry District that  
3 the proposed charge may reasonably be used to avoid rate increases to finance water  
4 main extensions and upsizing.” Although they expressed “general agreement with the  
5 rationale underlying the charge,” they had some specific concerns which we were  
6 directed to address in a revision within a year, which we did. Our revisions successfully  
7 addressed the Commission’s concerns, and our revised tariff was approved.

8

9 **Q. WHEN THE OIC WAS FIRST APPROVED IN 2002, WAS 807 KAR 5:090**  
10 **ALREADY IN EFFECT?**

11 A. Yes. In fact, in April of 2002, three months prior to our approval, the AG filed a brief  
12 in our case notifying the Commission that “It is clear the District is seeking approval of a  
13 system development charge tariff under an existing regulation addressing this type of  
14 mechanism.”

15

16 **Q. DID THE 2002 ORDER APPROVING THE OIC FOR THREE YEARS**  
17 **DIRECT THAT IN 2005 YOU MODIFY OR REPLACE THE OIC TO COMPLY**  
18 **WITH 807 KAR 5:090?**

19 A. No.

20

21 **Q. HOW DID YOU INTERPRET THE COMMISSION’S 2002 APPROVAL OF**  
22 **THE OIC?**

1 A. We thought we had made our case, and that the charge was seen by the Commission  
2 as an acceptable alternative methodology in keeping with the latitude and flexibility  
3 which Case 375 said was in the public interest. When we submitted the OIC in  
4 November 2001, the PSC had already submitted its proposed SDC regulation, so before  
5 they saw the OIC, the Commission had determined what they wanted the new regulation  
6 to require. In the LRC review phase of the promulgation of 807 KAR 5:090, the  
7 Commission stated that “the proposed regulation does not recognize any preferred  
8 methodology” and that an applicant could request a deviation from any of the  
9 regulation’s SDC requirements which were not necessary to that applicant’s  
10 methodology.

11

12 So we had good reasons to believe in 2002 that our rationale and approach had been  
13 judged to be an acceptable alternative SDC methodology, but that the Commission also  
14 wanted to make sure after three years that we were properly administering the operation  
15 of the program: that we were only charging the OIC when appropriate, that we were  
16 escrowing and accounting for the proceeds properly, that we were funding appropriate  
17 projects and making refunds where necessary.

18

19 **Q. WHAT HAPPENED IN 2005?**

20 A. For a long time, nothing. We had written a letter in July, expressing our hope that the  
21 yearly accountings and updated calculations we had submitted in keeping with the OIC  
22 requirements would allow the Commission to review and approve our charge. But we  
23 received no response, so we called Brent Kirtley, who suggested we actually resubmit the

1 tariff. We did so in August, but again there was no response, or even acknowledgement.  
2 At first we thought this was because the review was considered a low-priority formality  
3 due to our previous compliance with all the OIC reporting requirements. But finally in  
4 April of 2006 we wrote again. The Commission opened case 2006-00191 in May 2006,  
5 nine months after our tariff submittal.

6

7 **Q. WERE YOU SURPRISED BY THE NATURE OF THAT ORDER?**

8 A. Yes, very much so. The order began by misquoting a key sentence from the 2002  
9 approval order so that instead of requiring after three years a “a full review of the  
10 operation of the program,” it now claimed that in 2002 the Commission had “directed  
11 that the operation and reasonableness of the charge be reexamined after three years to  
12 determine if it should continue.”

13

14 It didn't seem possible that the Commission in 2002 would have authorized us to levy a  
15 charge for three years (and several hundred thousand dollars) without having first clearly  
16 established its reasonableness. It didn't seem possible that the property owners and  
17 developers in our District had been required to pay over a quarter million dollars to  
18 conduct a reasonableness experiment. We couldn't understand how the collection of  
19 these charges would shed any significant new light on the OIC's underlying rationale.  
20 And if the word “operation” in 2002 was intended to include reasonableness, we couldn't  
21 understand why it was thought necessary to modify the Commission's 2002 “operation of  
22 the program” directive by adding “reasonableness of the charge” in 2006.

1 If this sounds like hair-splitting and semantics, there is definitely nothing trivial about the  
2 expense and effort of complying with an exhaustive reexamination of the reasonableness  
3 of a charge which is commonsense, conservative, and cost-based. This second OIC case  
4 encompasses 79 interrogatories with numerous subsections, and ten appendices with  
5 almost 200 pages of documentation. It encompasses the September 13 hearing, and the  
6 preparation of a final brief addressing 6 additional interrogatories. The expenses are  
7 considerable, and they are being borne by the 6000 customers of the Henry District.

8

9 In Case 375 the Commission asked water utilities if they needed new rate mechanisms  
10 like SDCs to handle the costs of growth. About 85% said yes, but six years later the  
11 Henry District's charge is still the only SDC in Kentucky, and it is undergoing prolonged  
12 scrutiny. It is not unreasonable to suspect that the substantial costs and effort required in  
13 our situation are affecting the likelihood that other districts will decide to submit SDCs.

14

15 When Chairman Goss addressed the KRWA in 2004 he stated that extending service to  
16 the half-million Kentuckians who have no reliable water supply should be one of  
17 Kentucky's highest priorities. The approval of SDCs furthers that goal by requiring  
18 development to carry a fair share of the growth costs of larger lines, new tanks, and  
19 treatment capacity. This in turn frees up state grants to address the otherwise cost-  
20 ineffective extension of lines into those areas which still lack basic water service, areas  
21 which can often be low-income. To the extent that state grants are used in lieu of SDCs  
22 to fund capacity expansions for subdivisions and commercial developments, the goal of  
23 statewide water service is less attainable.

1 **Q. DISCUSS THE ISSUES IN CASE 2006-00191 WHICH SEEM TO HAVE**  
2 **GREATEST SIGNIFICANCE TO COMMISSION STAFF.**

3 A. Based on the interrogatories and the informal conference last fall, the primary issues  
4 are reasonableness, growth rate, depreciation, and benefits to existing customers.

5

6 Reasonableness:

7 807 KAR 5:090 states:

8 “The commission shall consider a proposed system development charge reasonable if the  
9 applicant demonstrates that the proposed charge: (1) Offsets an increase in cost to fund  
10 system expansion to accommodate new growth and demand; (2) Recovers only the  
11 portion of the cost of a system improvement that is reasonably related to new demand;  
12 and (3) Is based upon the cost of a new facility that will increase or expand capacity.”

13 The Henry District’s charge meets these three criteria by evaluating only projects which  
14 provide improvements to offset the demands of growth, thereby establishing a reasonable  
15 relation to new demand, and by basing its cost specifically on new facilities which  
16 increase capacity.

17

18 Case 375 states that alternative methodologies will be acceptable if they achieve a more  
19 reasonable result than standard incremental or equity approaches. HCWD2 has  
20 developed a conservative charge based on actual historical costs. By contrast, a standard  
21 incremental SDC is based on a 10 year capital improvement plan, which first estimates  
22 the number and type of new customers, then estimates how much water they will use,  
23 then, considering where this growth may occur, estimates how much infrastructure will

1 be required, and finally estimates the total future infrastructure cost. With exceptionally  
2 prescient professional estimates, assume each of these component projections may  
3 achieve a plus or minus 10% accuracy. Because the four estimates are interdependent, it  
4 is possible to have an actual final cost outcome which is  $(.9 \times .9 \times .9 \times .9) = .65$  of the  
5 CIP estimate, or an outcome which is  $(1.1 \times 1.1 \times 1.1 \times 1.1) = 1.45$  of the CIP estimate.  
6 This means the \$1000 per lot SDC should actually have been \$650 in the first case or  
7 \$1450 in the second. Estimates with plus or minus 15% accuracy would produce a range  
8 from \$500 to \$1750. It is not difficult to understand that the Henry District's cost-based  
9 OIC achieves a more reasonable result.

10  
11 The AWWA, in Chapter 28 of the M1 Rates Manual, states that "In considering the  
12 design and implementation of a system development charge, an analyst should:  
13 ...evaluate the underlying criteria important to a specific water system." This would  
14 seem to be very appropriate to HCWD2's situation. With reserve treatment capacity, but  
15 with small diameter lines limiting growth in the distribution system, the District has  
16 designed a methodology responsive to its system's specific requirements. Rates Manual  
17 M1 also suggests that incremental SDCs based on ten year capital improvement estimates  
18 are commonly updated at 3 to 5 year intervals. Although KAR 5:090 doesn't require  
19 such recalculations, the HCWD2 charge does. It is a cost-based rolling average, with  
20 regular database updates.

21  
22 Growth:

1 There appears to be held among some members of the Commission staff the conviction  
2 that SDCs are appropriate only if they have determined growth to be “significant.”  
3 However the PSC has endorsed the general principle of SDCs in Kentucky without  
4 establishing, either in Administrative Case 375 or in the consequent promulgation of 807  
5 KAR 5:090, any minimum growth rate threshold for SDCs, or any definition of  
6 “significant growth.” The three criteria for reasonableness in KAR 5:090 do not mention  
7 growth rate. Requiring some specific level of growth might impose precisely the kind of  
8 “rigid and inflexible standard” which the Commission in Case 375 deemed contrary to  
9 the public interest.

10

11 Further, the acceptability of the equity methodology to both the AWWA and to the PSC  
12 in Case 375 must mean that a growth rate which outpaces the district’s conventional  
13 funding mechanisms is clearly not a prerequisite for an SDC.

14

15 But even assuming that “normal” growth is intended by the PSC to be covered by general  
16 rates, how can the PSC approve or deny SDCs without first defining “significant”  
17 growth? Will growth be deemed normal if it represents the statewide or regional  
18 average, or if, despite being high relative to other districts, it is normal growth for the  
19 applicant district? Is it reasonable to require water districts to risk the considerable  
20 expense of preparing applications for SDCs and responding to PSC interrogatories and  
21 requests for documentation, when those districts cannot possibly know in advance  
22 whether their SDC will be denied by the imposition of the undefined standards of  
23 “significant” growth?

1

2 If the PSC requires a “significant” growth rate threshold for SDCs, it will create two  
3 unequal classes of water districts and customers in Kentucky. Districts without SDCs  
4 will require their existing customers to pay for growth in general rates, while districts  
5 with SDCs will exempt their existing customers from those same charges. But the  
6 impact of growth on a utility is cumulative. A system with annual growth of 3% for 8  
7 years will be faced with the same overall growth-necessitated infrastructure costs as a  
8 similar system with 8% growth for 3 years.

9

10 The actual costs of growth are not a direct function of growth rate. The need to expand  
11 capacity often depends entirely on where growth occurs within a system. And even  
12 identical growth rates in different systems can produce very different growth-necessitated  
13 expenses. A system with surplus capacity could incur no costs at all from growth, but a  
14 system nearing capacity (as many KY systems are) could incur high costs from much  
15 lower growth levels.

16

17 If “significant” growth is a requirement, what policy will the PSC follow if an SDC is  
18 approved, but the district’s growth rate subsequently diminishes? Will the PSC monitor  
19 growth and revoke an SDC if the district is only experiencing growth comparable to other  
20 districts whose SDCs were denied?

21

22 An SDC is a reasonable and prudent way for the district to be prepared for *potential*  
23 growth, cited as an appropriate reason for SDCs by the AWWA in Chapter 28 of their

1 M1 Rates Manual. Except for the time and expense of obtaining PSC approval, no harm  
2 is done by having an SDC in place in advance of “significant” growth.

3  
4 Finally, imposing threshold growth requirements is particularly inappropriate regarding  
5 the OIC. The mechanism by which the HCWD2 charge is calculated provides a  
6 reasonable offsetting cost per unit of usage, and does not rely on a growth-sensitive 10  
7 year capital improvement plan to calculate or to justify its charge. It treats all levels of  
8 growth equally and proportionately, and it is based on the recent average cost of  
9 increasing capacity, not on projections of the future. It is self-adjusting, and it remains  
10 fair and reasonable.

11

12 Depreciation:

13 On the first page of its final order in SDC Case 375, the Commission says that “SDCs  
14 may keep a utility from withdrawing funds from its depreciation accounts to pay for  
15 capacity expansions or other construction.” The Commission would encourage precisely  
16 the opposite practice if it instructs utilities that SDCs are not needed because depreciation  
17 should fund growth.

18

19 Considering forty years of inflation, it is improbable that recovered depreciation would  
20 be adequate even to replace a worn out 6” line with a new 6” line. Depreciation therefore  
21 cannot possibly contribute at all to the *additional* cost increment needed to install a 12”  
22 line necessitated by growth. The \$5 per foot recovered in depreciation cannot stretch  
23 enough to cover the current replacement cost of \$10. Those who contend that it is

1 possible to stretch that \$5 even further to provide \$25 per foot for the new 12” line have  
2 not only expanded the definition and purpose of depreciation, they have developed a new  
3 form of mathematics.

4

5 The anti-SDC argument that there exist other ways (such as an expanded definition of  
6 depreciation) to incorporate growth-necessitated costs into general rates is not an  
7 argument for the fairness of doing so, only the expediency. An ethically neutral-  
8 sounding term like “recoverable” evades the fundamental issue of fairness. Tapping fees,  
9 late payment fees, and other separate charges produce levels of revenue which might be  
10 recoverable by inclusion in general rates with slight effect. These fees are paid  
11 separately because of fairness.

12

13 When depreciation funds are used to pay for capacity expansion necessitated by growth,  
14 Peter is being robbed to pay Paul, under-funding the actual replacement of worn out  
15 facilities. If the reverse situation occurs, and SDC proceeds are used simply to replace  
16 age-deteriorated infrastructure, this is a serious and unacceptable misuse of funds. But  
17 the legitimate justifications for a system development charge cannot be discredited by  
18 presupposing that the status of a district’s depreciation recovery will result in the  
19 misallocation of SDC proceeds. Henry District’s OIC requires submittal to the PSC of a  
20 listing of all eligible projects and a yearly accounting of all expenditures.

21

22 Although it is generally intended (and has been the case) that the new larger OIC-funded  
23 lines parallel, not replace, existing lines, nevertheless when those older lines do wear out,

1 the OIC line will then partially function as their replacement. HCWD2 therefore would  
2 consider making a depreciation adjustment to its OIC calculation. If the larger OIC line  
3 parallels an existing line which is near the end of its useful life, 100% of the depreciation  
4 expense of that line would be deducted from the cost of the new OIC line before it is  
5 entered into the OIC project database. Conversely, if the existing line is nearly new and  
6 remains in service, it will reach the end of its serviceability at about the same time as will  
7 the OIC line. Therefore the OIC line would not replace the smaller line at all, and no  
8 deduction would be made to the OIC calculation. If the existing line remains in service  
9 with 50% of its useful life remaining, then 50% of its depreciation expense would be  
10 deducted.

11

#### 12 Benefits to Existing Customers

13 The Case 2001-00393 Order approving our charge directed that “Within 12 months from  
14 the date of this Order, Henry District shall amend its Offsetting Improvement Charge  
15 tariff to include a provision for a long-range construction plan; a method to determine the  
16 *benefits existing customers receive from any system improvements*; and criteria to be used  
17 for locating or upsizing mains.” (Emphasis added) Henry District evaluated the benefits  
18 from system improvements and added language which amended the OIC and clarified  
19 that no net benefit to existing customers would occur.

20

21 However in Case 2006-00393, the Commission staff has raised the issue of other benefits  
22 which may accrue to existing customers as a result of *growth itself*. Staff has suggested  
23 that the improved overall revenue efficiency due to economy of scale is exclusively due

1 to new customers, although new customers when considered exclusively would constitute  
2 a very inefficient customer base. Staff has also suggested that the benefits of this overall  
3 economy of scale (a scale which is actually due as much to existing customers as to new  
4 ones) should not be used in ways which benefit all customers, but should instead be used  
5 exclusively to pay the infrastructure costs of growth. In effect, all customers will pay  
6 inflated rates which fund the infrastructure costs of growth, contrary to the basic rationale  
7 of the SDC.

8

9 Any discussion of hypothetical growth-induced revenue surplus is shortened  
10 considerably by a reality check of HCWD2's actual net income per customer, which has  
11 declined despite growth. Further, we have estimated that by not including supply,  
12 treatment, and storage, the OIC excludes about \$600 per new customer, or about a 40%  
13 reduction. Benefits from growth would be dramatic indeed if they exceeded this amount.

14

15

16 "The available evidence shows that development does not cover new public cost; that is,  
17 it brings in less revenue for local governments than the price of serving it." *Alan*

18 *Altschuler and Jose A. Gomez-Ibanez, Regulation for Revenue: A Political Economy of*  
19 *Land Use Exactions (Washington: Brookings Institute; Cambridge: Lincoln Institute of*  
20 *Land Policy, 1993), p. 77.*

21

22 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

23 A. Yes.